UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

ISO New England, Inc. Docket No. ER07-546-001

ORDER GRANTING AND DENYING REHEARING
AND DENYING CLARIFICATION

(Issued July 25, 2007)

1. In this order, the Commission grants and denies rehearing and denies clarification of its earlier order[1] conditionally accepting the market rules proposed by ISO New England, Inc. (ISO-NE) to implement New England's Forward Capacity Market (FCM).

I. Background

2. As discussed in prior orders in this proceeding,[2] as a means of ensuring reliability, for many years ISO-NE has imposed an installed capacity (ICAP) requirement on load-serving entities, requiring them to procure specified amounts of ICAP based on their peak loads plus a reserve margin. Beginning in 1998, ISO-NE began operating a bid-based market for ICAP.[3] In 2000, as the region began to develop wholesale power markets and utilize market-based rates, flaws became apparent in the ICAP market, and the Commission allowed ISO-NE to replace the ICAP auction mechanism with an administratively-determined ICAP deficiency charge. Further, due to concerns regarding the number of generators seeking cost-of-service Reliability Must Run (RMR) contracts and the effect that widespread use of such contracts could have on the competitive

[1] *ISO New England*, 119 FERC ¶ 61,045 (2007) (April 16 Order).

[2] *Devon Power LLC*, 111 FERC ¶ 63,063 (2005) (Initial Decision); *Devon Power LLC*, 115 FERC ¶ 61,340 (2006) (FCM Order), *order on reh'g*, 117 FERC ¶ 61,133 (2006) (FCM Rehearing Order).

[3] *See New England Power Pool*, 83 FERC ¶ 61,045 at 61,263 (1998).

market, the Commission directed ISO-NE "to file no later than March 1, 2004 for implementation no later than June 1, 2004, a mechanism that implements location or deliverability requirements in the ICAP or resource adequacy market . . . so that capacity within [congested areas] may be appropriately compensated for reliability."[4] Accordingly, ISO-NE submitted a filing seeking to implement a locational ICAP market in New England, and after a hearing before an Administrative Law Judge and extensive further proceedings, the parties arrived at a settlement with regard to that filing (Settlement Agreement), which the Commission substantially approved in the FCM Order and FCM Rehearing Order.

3. On February 15, 2007, as required by the Settlement Agreement, ISO-NE filed the revisions to its market rules required to implement the Settlement Agreement.

4. The proposed rules establish that ISO-NE will conduct an annual auction to procure capacity. This annual auction (Forward Capacity Auction)[5] will be conducted three-plus years in advance of the period during which capacity will actually be supplied.[6] The period between the Forward Capacity Auction and the supply commitment period will provide a planning period for new entry, so that potential new capacity suppliers (capacity resources) may participate in the Forward Capacity Auction and compete with existing resources. Each Forward Capacity Auction applies to a commitment period that corresponds to ISO-NE's June-to-May Power Year. Any resource that clears the Forward Capacity Auction is obligated to supply capacity during the applicable supply commitment period, *i.e.*, the year beginning June first. "Clearing" the Forward Capacity Auction means that the capacity resource was selected in the auction, and then must assume a supply obligation for the supply commitment period to which the Forward Capacity Auction corresponds. Forward Capacity Auctions are designed as "descending clock" auctions. The auction administrator announces a Starting Price, at which all capacity is presumed to be offering into the auction. Prices will "tick down" or descend from the Starting Price in a series of rounds, with resources being withdrawn from the auction (*i.e.*, de-listing) in each round. The auction will conclude

[4] *Devon Power LLC*, 103 FERC ¶ 61,082 at P 37 (2003)

[5] Capitalized terms used but not otherwise defined in this order have the meanings ascribed to them in ISO-NE's Transmission, Markets and Services Tariff (the tariff), the Second Restated New England Power Pool Agreement, and the Participants Agreement. *See* Transmittal, February 15 filing, at 1 fn. 4.

[6] The FCM also entails additional reconfiguration auctions to be conducted in the time between the Forward Capacity Auction and the supply commitment period. For example, the initial Forward Capacity Auction will be held in February 2008 and will procure capacity for the period of June 1, 2010 to May 31, 2011.

when the number of megawatts (MWs) offered equals the number of MWs that need to be bought. The Settlement Agreement stipulated that in each Forward Capacity Auction, ISO-NE will procure 100 percent of the amount of capacity needed in the New England control area and within each capacity zone.[7] New England's Load Serving Entities (LSEs) are responsible for paying for the amount of capacity determined by ISO-NE to be necessary for the system.

5. In its April 16 Order, the Commission largely approved the new rules proposed at sections III.13.1 and III.13.2 of ISO-NE's tariff, which establish the process through which capacity resources qualify for participation in Forward Capacity Auctions, and the mechanics of the Forward Capacity Auction.

6. Section 13.1 addresses the rules and procedures associated with qualifying resources for participation in the FCM. Each resource that seeks to sell (offer) capacity into the FCM must qualify as one of several resource types, including: 1) a new generating capacity resource; 2) an existing generating capacity resource; 3) an import capacity resource, existing or new; or 4) a demand resource, existing or new.[8]

7. Existing capacity resources are assumed to participate, but may remove themselves from participation in the Forward Capacity Auction. This is accomplished through the submission of a de-list bid. Four types of de-list bids[9] must be submitted to ISO-NE in advance of the Forward Capacity Auction, during the qualification process; the fifth type (Dynamic De-List Bids) may change during the auction. If any of the pre-auction de-list bids are greater than a specified price threshold, that bid will be reviewed by ISO-NE's Market Monitor, which may require the capacity resource to submit additional information for review. ISO-NE is required to submit a filing to the Commission at least three months prior to each Forward Capacity Auction in which it will, among other things, set forth its findings on the de-list bids that have been submitted, those that have been accepted and those that have not.

1. De-listing provisions for existing capacity resources

8. The Settlement Agreement permits existing capacity resources to forego receiving capacity revenues for a commitment period by submitting bids to de-list from the

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[7] Settlement Agreement at 11.I.A.

[8] Load serving entities may designate resources as "Self-Supplied," which results in an offset to the load serving entity's share of its capacity obligation.

[9] Permanent De-List Bids, Static De-List Bids, Export Bids, and Administrative Export De-List Bids.

capacity market. A de-listed resource has no obligation to bid into the Day-Ahead and Real-Time energy markets for the period for which it is de-listed, and does not have to honor ISO-NE's requests to reschedule maintenance. All pre-auction de-list bids submitted during the qualification process and accepted by ISO-NE are binding and shall be entered into the Forward Capacity Auction as described in section III.13.2.3.2(b).

9. De-list bids that are above certain price thresholds specified in the Settlement Agreement will be subject to review by ISO-NE's Market Monitor. The proposed rules on FCM provide for Market Monitor review of each Static De-List Bid, each Export Bid above 0.8 times Cost of New Entry.[10] Cost of New Entry values for subsequent Forward Capacity Auctions will be calculated based on the clearing prices from previous successful auctions and each Permanent De-List Bid above 1.25 times Cost of New Entry. This review is designed to determine whether these bids are consistent with the existing generating capacity resource's net risk-adjusted going forward costs.[11] Sufficient documentation and information must be included in the existing capacity qualification package to allow ISO-NE's Market Monitor to make such determinations. A Permanent De-List Bid priced between 0.8 times Cost of New Entry and 1.25 times Cost of New Entry will be presumed competitive unless the Market Monitor determines that the bid is an attempt to manipulate the Forward Capacity Auction.

10. Finally, existing generating capacity resources may submit de-list bids during the auction itself, by submitting a Dynamic De-List Bid. Dynamic De-List Bids are submitted during the auction at any price below 0.8 times Cost of New Entry. Such bids are not submitted to ISO-NE during the qualification process and therefore are not subject to review by the Market Monitor during the qualification process.

11. No later than 120 days before the Forward Capacity Auction, ISO-NE will send notification to existing capacity resources indicating whether the resources' de-list bids were accepted. Each accepted de-list bid will be binding and shall be entered into the Forward Capacity Auction. The qualification determination will not include the results of the reliability review.

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[10] Each modeled capacity zone will have a Starting Price equal to two times the Cost of New Entry associated with that capacity zone. Under section III.13.2.4, Cost of New Entry for all capacity zones in the first Forward Capacity Auction will be $7.50/kW-month, as the parties agreed in the Settlement Agreement at 11.III.F.

[11] Section III.13.1.2.3.2.1. These thresholds are expressly provided for in the Settlement Agreement. *See* Settlement Agreement at section 11.III.D.

2. Publication of offer and bid information

12. The proposed rules state that each Permanent De-List Bid will be posted no later than three business days after the existing capacity qualification deadline.[12] This posting will include the name of the resource, the quantity, the price, and load zone in which the resource is located. For Static De-List Bids, ISO-NE will post the quantity, price, and load zone no later than three business days after the same deadline. ISO-NE will post the name of submitter, quantity, and interface of export bids and administrative export bids, and of offers of new import capacity resources by the same deadline. ISO-NE will post the resource name, quantity, price, and load zone in which the resource is located of resources whose Static De-List Bid or Permanent De-List Bid above 0.8 times Cost of New Entry was approved. Personnel from state commissions will be provided confidential access to full information about posted Static De-list Bids and Permanent De-List Bids, upon request, pursuant to section 3.3 of the ISO-NE Information Policy.

3. Timeline

13. Beginning with the timeline for the commitment period commencing on June 1, 2016 (the seventh Forward Capacity Auction) and for each commitment period thereafter, the deadlines will be consistent for each commitment period, as follows: First, each commitment period will begin in June. Second, the new capacity Show of Interest submission window will be the November through December period that is approximately four years and six months before the beginning of the commitment period. Third, the existing capacity qualification deadline will be in April just over four years before the beginning of the commitment period. Fourth, the new capacity qualification deadline will be in June just under four years before the beginning of the commitment period. Finally, the Forward Capacity Auction for the commitment period will begin in February, approximately three years and four months before the beginning of the commitment period.

14. The time from the first day of the Forward Capacity Auction to the first day of the commitment period is 28 months for the first Forward Capacity Auction. That length of time extends to 40 months, pursuant to the Settlement Agreement, by the seventh Forward Capacity Auction. The market rules provide for a review of the issue and possible revisions to the schedule to increase the length of the planning period more quickly.

15. ISO-NE states that the Settlement Agreement contemplated a 40-month planning period between each Forward Capacity Auction and the beginning of the associated commitment period. However, the proposed schedule for the first six Forward Capacity

[12] Section III.13.1.8.

Auctions entails a shorter planning period for each of those Forward Capacity Auctions—increasing from 28 months to the 40 months referenced in the Settlement Agreement.

4. Conduct of Forward Capacity Auction

16. Section III.13.2.3 of the proposed rules on FCM addresses how Forward Capacity Auctions are conducted. The proposed tariff is sub-divided into separate steps:

- Step 1: Announcement of Start-of-Round and End-of-Round Prices
- Step 2: Compilation of Offers and Bids
- Step 3: Determination of the Outcome of Each Round

a. Step 1: Announcement of Start-of-Round and End-of-Round Prices

17. Each Forward Capacity Auction will begin at a predetermined price – the Starting Price – which is two times Cost of New Entry.[13] There may be differing values of Cost of New Entry for these separate zones. The first round of the Forward Capacity Auction will begin at the Starting Price and conclude at the End-of-Round Price. After the first round, the Start-of-Round price for the next round will equal the End-of-Round Price from the previous round.

b. Step 2: Compilation of Offers and Bids

i. Offers from New Capacity Resources

18. The proposed rules require that new generating, import and demand resources that have been qualified to participate offer their full Qualified Capacity at the Starting Price.[14] New capacity resources are free to offer less or no capacity at prices below the Starting Price, subject to the other requirements of the proposed rules. The Settlement Agreement provides that the Market Monitor will review new capacity resources' offers below a specific level (0.75 times Cost of New Entry).[15] New capacity resources must submit those offers to ISO-NE in their qualification packages, along with supporting information.

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[13] Section III.13.2.3.1.

[14] Section III.13.2.3.2(a)(i).

[15] Settlement Agreement at 11.III.H.1.

ii. Bids from Existing Capacity Resources Accepted in Qualification

19. As discussed earlier in this order, an existing capacity resource may submit de-list bids in order to remove itself from participation in the Forward Capacity Auction

iii. Existing Capacity Resources without Bids or whose Bids were not Accepted in Qualification

20. An existing capacity resource that did not seek to de-list prior to the auction will be bid automatically into each round of the Forward Capacity Auction at its summer Qualified Capacity. In order to remove itself from participation in the Forward Capacity Auction, such a resource must submit a Dynamic De-List Bid during the Forward Capacity Auction itself. A Dynamic De-List Bid does not require prior approval of ISO-NE's Market Monitor. In any round of a Forward Capacity Auction, when prices are 0.8 times Cost of New Entry or lower, any existing resource, other than those designated as self-supply, may submit a Dynamic De-List Bid.[16]

c. Step 3: Determination of the Outcome of Each Round

21. The proposed rules state that the auctioneer will use offers and bids submitted in a particular round to construct aggregate supply curves.[17] The auctioneer will construct a supply curve for the New England Control Area and for each modeled capacity zone included in the round. Generally, the information that is used to construct such curves will include the amount of capacity offered in capacity zones at prices within the round, the Installed Capacity Requirement, the Local Sourcing Requirement of any import-constrained zones, and the Maximum Capacity Limit of any export-constrained zones. On the basis of these aggregate supply curves, which reflect total system capacity, the auctioneer will determine the outcome of the round for each modeled capacity zone. Before the Forward Capacity Auction, capacity zones will be determined by ISO-NE based on an identification of transmission limits that may bind and whether those limits are expected to bind.[18] However, if a modeled constraint does not bind in the Forward Capacity Auction, the price in that zone will be the same as the price for an adjacent capacity zone. The final set of capacity zones that result from the Forward Capacity Auction will apply to all reconfiguration auctions applicable to that commitment period.

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[16] Section III.13.2.3.2(d).

[17] Section III.13.2.3.3.

[18] Section III.13.2.3.4.

5. Starting Price and Cost of New Entry Determination

22. Each modeled capacity zone will have a Starting Price equal to two times the Cost of New Entry associated with that capacity zone. Under section III.13.2.4, Cost of New Entry for all capacity zones in the first Forward Capacity Auction will be $7.50/kW-month.[19] Cost of New Entry values for subsequent Forward Capacity Auctions will be calculated based on the clearing prices from previous successful auctions. After three successful Forward Capacity Auctions have been conducted for a given capacity zone, the proposed rules provide that the Cost of New Entry for that capacity zone in a Forward Capacity Auction will be the sum of 70 percent of that capacity zone's Cost of New Entry from the previous Forward Capacity Auction plus 30 percent of that capacity zone's clearing price from the previous Forward Capacity Auction.

6. Treatment of Specific Offers and Bids in Forward Capacity Auction

23. Offers from new generating, import and demand resources will "clear" the Forward Capacity Auction if the descending clock auction stops at a price at or above that specified in the offer.[20] Unless rejected for reliability reasons, a Permanent De-List Bid will clear[21] the Forward Capacity Auction if the clearing price is less than the price specified in the Permanent De-List Bid. The amount of capacity that is permanently de-listed capacity will be replaced either in the current Forward Capacity Auction or in subsequent annual reconfiguration auctions.[22] The clearing price in the Forward Capacity Auction will determine in which auction the de-listed capacity is replaced.

24. The proposed rules generally provide that, except where rejected for reliability reasons, a Static De-List Bid or an Export Bid will clear the Forward Capacity Auction if the clearing price is less than the price specified in the bid.[23] Similar to the provisions for Permanent De-List Bids, the Forward Capacity Auction clearing price will determine whether the de-listed capacity will be replaced in the Forward Capacity Auction or in subsequent annual reconfiguration auctions. An Administrative Export Bid will clear in

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[19] Settlement Agreement at 11.III.F.

[20] Section III.13.2.5.

[21] In contrast to offers to sell capacity, a Permanent De-List Bid clearing the market means that the existing capacity resource that submitted that bid no longer has an obligation to supply capacity.

[22] Section III.13.2.5.2.

[23] Section III.13.2.5.2.2.

the Forward Capacity Auction regardless of clearing price and regardless of whether there is inadequate supply or insufficient competition in the capacity zone. The proposed rules state that a Dynamic De-List Bid will clear in the Forward Capacity Auction if the clearing price is less than the price specified in the bid.

7. Rejection of de-list bids for reliability reasons

25. Section III.13.2.5.2.5 addresses de-list bids that ISO-NE rejects for reliability reasons. ISO-NE will determine that an existing capacity resource is needed for reliability if the absence of that existing capacity resource would result in a violation of any criteria developed by the North American Electric Reliability Corporation or the Northeast Power Coordinating Council, or ISO-NE system rules.

26. Where ISO-NE has determined that some or all of the capacity associated with a de-list bid is needed for reliability reasons, then that capacity will not clear in the Forward Capacity Auction, and that resource will be notified following the Forward Capacity Auction.[24] Following the last reconfiguration auction, if ISO-NE determines that the reliability concern has not been addressed, then the resource will become a listed resource for the commitment period and will be compensated at a just and reasonable price, as determined by the Commission.[25] The proposed rules at present do not resolve the determination of a just and reasonable rate, the form of any reliability agreement or the process for obtaining a reliability agreement.

a. Alternative Price Rule

27. The Settlement Agreement provided for an Alternative Price Rule to be employed under certain circumstances. The Alternative Price Rule is intended to remove the incentive for load to self-supply their own capacity for the sole purpose of depressing capacity prices. The settlement provides for an alternative price rule that resets the FCA clearing price under certain conditions. In cases where the number of megawatts of required new entry is less than the megawatts of out of market purchases,[26] the capacity price is based on the lowest rejected offer submitted by a new entrant. The rule was designed to lower investment risk by mitigating price volatility in Forward Capacity

[24] Section III.13.2.5.2.5.

[25] Section III.13.2.5.2.5(b).

[26] When at least some of the offers from new capacity or imports are below .75 times the Cost of New Entry and the Market Monitor concludes that such low offers are not consistent with long run average costs, opportunity costs, or other reasonable economic measures, capacity submitting such bids is deemed to be “out-of-market.”

Auctions and to remove the incentive to self-supply capacity in order to depress capacity prices.

II. Requests For Rehearing, And Answers

28. ISO-NE, NRG Companies (NRG) and H.Q. Energy Services (U.S.) (HQUS) filed timely petitions for rehearing. The New England Conference of Public Utility Commissioners (NECPUC)[27] submitted a request for rehearing and motion for clarification. Brookfield Energy Marketing (Brookfield) submitted a comment supporting HQUS' request for rehearing, which the Commission will treat as a request for rehearing on Brookfield's part.

29. Subsequently, ISO-NE, Capacity Suppliers,[28] Milford Power Company, LLC and NRG Companies (Milford/NRG), the Interconnection Rights Holders Management Committee (IRH Management Committee) and NSTAR Electric and Gas Corporation (NSTAR) submitted answers to the requests for rehearing and clarification. HQUS subsequently submitted a response to the answers filed by the IRH Management Committee and NSTAR, and NSTAR filed a response to the response submitted by HQUS.

III. Discussion

30. As an initial procedural matter, Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2006), prohibits an answer to a request for rehearing or an answer to an answer unless otherwise ordered by the decisional authority. We will accept the parties' answers to the petitions for rehearing, and HQUS' answer to the IRH Management Committee and NSTAR's answers, because they have provided information that assisted us in our decision-making process. We are not persuaded to accept NSTAR's response to HQUS' answer, and therefore reject it.

31. Substantively, the Commission grants rehearing as to the question of when ISO-NE should notify a de-list bidder whose bid is rejected for reliability reasons, denies all remaining requests for rehearing, and denies the requests for clarification, as follows.

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[27] NECPUC's request for rehearing was joined by the Connecticut Department of Public Utility Control, the Vermont Department of Public Service, and the Connecticut Office of Consumer Counsel.

[28] Capacity Suppliers note that, for purposes of this filing, they consist of Mirant Energy Trading, LLC; Mirant Canal, LLC; Mirant Kendall, LLC; Boston Generating, LLC; and FPL Energy, LLC.

A. The Commission properly required that, when ISO-NE's market monitor rejects a resource's de-list bid, it must disclose its determination of appropriate costs to the generator and allow the generator to submit a revised de-list bid.

32. Under the market rules accepted in the Commission's April 16 Order, the FCM permits both new and existing resources to offer to provide capacity to the New England market. As noted above, existing resources automatically participate in the auction unless they submit de-list bids – *i.e.*, the price at which a resource indicates that it is no longer willing to provide capacity to the market, and withdraws its capacity from the auction. If the resource lacks market power, its de-list bid should represent that resource's net risk-adjusted going forward and opportunity costs of providing service.

33. In an area with capacity constraints, however, an existing resource could potentially exercise market power by offering to de-list at a price that, in fact, is greater than the resource's going forward costs (*i.e.*, engaging in economic withholding). To address this potential for market power, the Settlement Agreement imposed certain requirements on the de-list bids of existing resources. Specifically, the Settlement Agreement required that any Static De-List Bid above 80 percent of the Cost of New Entry, and any Permanent De-List Bid above 125 percent of the Cost of New Entry, must be submitted (along with supporting justification) to ISO-NE's internal market monitor for review in advance of the auction.[29] (De-list bids below these threshold levels need not be submitted to the market monitor for review.)

34. To implement these requirements, ISO-NE proposed that if the monitor concluded that a de-list bid was not justified, the bid would be rejected and the resource would be included in the market as a price taker (*i.e.*, at a de-list bid of $0).[30] This rule would require that, if the auction cleared at a higher price than the resource's de-list bid, the resource would nevertheless be required to supply capacity at that price. The proposed rules also provide that the Market Monitor must provide an explanation of why each such de-list bid was rejected in an informational filing to be made with the Commission no less than 90 days before the first day of the Forward Capacity Auction.

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[29] A Permanent De-List Bid is a bid to remove the resource from capacity obligations during the delivery year, and to permanently preclude the resource from offering its capacity to meet any future capacity obligation in New England. A Static De-List Bid is a bid to remove the resource from any capacity obligations only during the delivery year; thus, a Static De-List Bid would not preclude the resource from offering its capacity into future capacity auctions.

[30] *See* proposed rules at section III.13.1.2.3.2.1.1.

35. Several protestors argued that ISO-NE's proposal would force resources to offer capacity below their costs. The protestors argued that the monitor and the resource owner may often disagree on a few cost components but may agree on the level of most cost components. In such instances, they stated, it was unreasonable to force a resource to accept a price below a level that even the monitor concluded was the resource's cost. In its April 16 Order, the Commission agreed with the protestors and required ISO-NE to revise the rule. The Commission stated:

> [I]f the price that clears in the Forward Capacity Auction is greater than 0.8 times Cost of New Entry, but still below the Market Monitor's determination of the resource's costs, the resource would be forced to provide capacity at a price that both the Market Monitor and the generator agree is below the costs for that resource. In the Commission's example,[[31]] if the capacity price cleared at $8.25/kW-month, the resource would not be allowed to exit the market and would be forced to offer capacity at a price $0.25/kW-month below the cost-appropriate level determined by the Market Monitor and affirmed by the Commission. The resource would not have the option of leaving the market, despite the fact that the clearing price was lower than its costs. This would be an unjust and unreasonable result.[32]

36. Therefore, the Commission required that the Market Monitor must disclose the results of its review, including all cost components and appropriate input levels used in

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[31] The Commission provided the following example (April 16 Order at P 118):

Suppose an existing generating capacity resource submits a Static De-List Bid of $9.00/kW-month, or exactly 0.9 times Cost of New Entry. Since the Static De-List Bid is greater than the mitigation threshold of 0.8 times Cost of New Entry, the Market Monitor would undertake a review of that resource's de-listing bid. If, after due consultation with the resource, the Market Monitor determines that a more appropriate level for that the resource's Static De-List Bid would be $8.50/kW-month, or 0.85 times Cost of New Entry, the Market Monitor would then submit an informational filing to the Commission 90 days prior to the auction containing the reasoning and cost support of rejecting the $9.00/kW-month Static De-List Bid. If the Commission agrees with the Market Monitor that $8.50/kW-month Static De-List Bid is a more accurate reflection of the affected resource's costs, then under the proposed FCM rules, the Static De-List Bid's rejection would be upheld, and the resource would be entered into the Forward Capacity Auction as a price taker.

[32] April 16 Order at P 119.

its mitigation formula, to the affected resource. We further required ISO-NE to amend the rules to allow existing resources whose de-list bids were determined to be inconsistent with their net risk-adjusted going forward and opportunity costs, as determined by the Market Monitor, to be allowed to submit revised de-list bids consistent with the costs determined by the Market Monitor.[33] We stated:

> This requirement will provide the existing generating capacity resource with the option of submitting a revised de-list bid consistent with the Market Monitor's determination and would prevent any possibility of confiscatory ratemaking.[34]

37. The Commission required ISO-NE to revise its rules to provide the resource with the option of submitting a revised de-list bid consistent with the Market Monitor's determination, subject to Commission review in the planned informational filing to be made 90 days before the Forward Capacity Auction. We further required that the informational filing should include cost support for all cost components of the Market Monitor's determination, cost support for the existing generating capacity resource's original de-list bid, and an explanation of the difference between the Market Monitor's cost determination and that of the existing generating capacity resource.[35]

1. Arguments on rehearing

38. ISO-NE and NECPUC request rehearing of this aspect of our April 16 Order, on several grounds.

39. First, ISO-NE asserts that the Commission erred in its treatment of a rate that ISO-NE filed pursuant to section 205 of the Federal Power Act (FPA).[36] ISO-NE states that under section 205, the Commission's inquiry is limited to whether the rates proposed by a utility are reasonable, and this inquiry does not extend to determining whether a proposed rate schedule is more or less reasonable than alternative rate designs. Thus, ISO-NE argues that, by proposing a different rate, the Commission goes beyond its power under section 205.[37]

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[33] *Id.* at P 120.

[34] *Id.*

[35] *Id.* at P 121, n. 83.

[36] 16 U.S.C. § 824d (2000).

[37] ISO-NE request for rehearing at 5.

40. ISO-NE then states that the Settlement Agreement recognized that existing resources could exercise market power over the clearing price, and provided that under the market rules, the Market Monitor would "review and reject" de-list bids that were inconsistent with a resource's costs.[38] ISO-NE views the April 16 Order as violating the Settlement Agreement. Moreover, ISO-NE states that the April 16 Order greatly expands the role of the Market Monitor in contravention of Commission policy, because it would require the Market Monitor to fashion a remedy for an excessive bid. ISO-NE states that this ruling violates Commission policy. Additionally, ISO-NE argues, our ruling would improperly shift the burden of proof regarding a resource's just and reasonable de-list bid from the resource itself to the Market Monitor, despite the fact that the generator, not the Market Monitor, has possession of all the relevant data.

41. ISO-NE and NECPUC state that our requirement that ISO-NE include in its annual informational filing a proper de-list bid for a generator whose bid has been rejected effectively relieves the generator of its obligation to prove that its de-list bid is consistent with its going forward and opportunity costs. ISO-NE further asserts that the Commission has placed the Market Monitor in the position of performing a cost of service analysis in order to determine that a bid is excessive, and in essence refashioning the bid. ISO-NE asserts that imposing this responsibility on the Market Monitor is inconsistent with the circumscribed role that the Commission has prescribed for market monitors in other contexts – namely, a role that prohibits the monitor from providing a remedy for the exercise of market power and instead requiring that the monitor refer the matter to the Commission for an appropriate remedy.

42. ISO-NE further states that, contrary to the Commission's view, the Market Monitor's review will not result in a substitute number for each cost component of the de-list bid, which can then be presented to the Commission as the "correct" number. Rather, ISO-NE represents, under its proposed rules, the Market Monitor will review cost components and, using a relatively mechanical formula reflecting fuel costs and heat rates in the energy market, determine broadly whether they are within a range of reasonableness. In contrast, the Commission would require the Market Monitor to derive costs at a significant level of detail, in some cases at a level more suitable for cost-of-service ratemaking. This is particularly true of opportunity costs, which, ISO-NE asserts, are generally too varied and involve subjective and idiosyncratic factors to be incorporated into a single equation. ISO-NE states that even if the Market Monitor were to use expert consultants to appraise a resource's opportunity costs, those appraisals will be subjective and may well differ. It further notes that the Commission errs in assuming that all costs could be found within a "mitigation formula."

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[38] *Id*. at 4 n. 12, *citing* Explanatory Statement to the Settlement Agreement at 11.

43. ISO-NE also challenges the Commission's conclusion that the proposed rules could result in generators not being allowed to recover their costs. ISO-NE states that its proposed rule already gives generators adequate time and opportunity to provide all their costs to the Market Monitor and to provide any necessary explanations (in addition to ultimately seeking Commission review of de-list bids rejected by the Market Monitor).[39] Thus, ISO-NE contends, the proposed rules provide safeguards against confiscatory ratemaking.

44. ISO-NE additionally argues that the Commission's ruling may facilitate the exercise of market power, because it provides a generator with multiple chances to modify its de-list bid, and thus, it removes all risk of initially overstating its costs. ISO-NE states:

> At present, there are about 33,000 megawatts of existing capacity receiving capacity credit. The incremental need for capacity to meet the Installed Capacity Requirement each year is likely to be between 500 to 1000 megawatts of capacity per year. If the de-list rules, as proposed, were not in place, a generating company with a large portfolio would have a strong incentive to withhold a relatively small amount of existing capacity to force the purchase of additional new capacity to increase the price in the FCM. For example, if existing generators are able to de-list as little as 200 megawatts of capacity, the need for new capacity would increase by at least 20 percent.[40]

45. ISO-NE then reiterates its view that the Commission's ruling would actually increase the potential for market manipulation. Under the April 16 Order, a generator seeking to de-list must submit a bid in its qualification package which will be reviewed by the Market Monitor. However, the Market Monitor may only decrease (but not reject) its de-list bid, the generator will be free to inflate its initial bid. Then, since the Market Monitor must itself establish what it considers an appropriate bid, the generator is free to accept that later bid as well. ISO-NE asserts that because the generator will never be forced to participate in the auction as a price taker, the generator has no incentive not to inflate its initial bid above its actual costs (and, presumably, anticipating that the Market

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[39] As ISO-NE notes, its proposed rules provide for the ability to comment on or challenge any of the determinations contained in the informational filing, and allot 75 days after the date of the informational filing for the Commission to direct the ISO to modify its determinations in conducting the Forward Capacity Auction, *see* ISO-NE request for rehearing at 21 n.52, *citing* proposed market rules at section III.13.8.1(b).

[40] ISO-NE request for rehearing at 22-23.

Monitor will be insufficiently knowledgeable to detect that inflation). ISO-NE states that, "[i]ndeed, the generator's acceptance of a lower [Market Monitor-determined] de-list bid is *prima facie* evidence that the initial bid was inflated and represents an attempt to exercise market power."[41] NECPUC similarly argues that the Commission's ruling in the April 16 Order could potentially substitute the Market Monitor's judgment for every de-list bid, so that, in essence, the Market Monitor will be engaging in cost-of-service ratemaking.

46. Finally, ISO-NE states that the April 16 Order is inconsistent with the Commission's policy statement on market monitors,[42] in that it contravenes the Commission's policy that market monitors should provide incentives to generators to provide service at the least cost possible. NECPUC argues that, similarly, the Commission does not need to provide incentives for resources to participate in the Forward Capacity Auction at all (or rather, to concern itself with providing disincentives to participate),[43] because all the resources who entered into the Settlement Agreement have already committed either to participate in the auction, or to submit de-list bids.

47. NECPUC further argues that, if the Commission does not grant rehearing, it should modify its prior ruling to require ISO-NE to file all the generators' supporting materials with the Commission.

48. In their answer to ISO-NE's and NECPUC's petitions for rehearing, Milford/NRG disagree with the assertion that in the April 16 Order the Commission is exceeding its powers under section 205. Rather, according to Milford/NRG, the Commission has specifically found ISO-NE's proposal to be unjust and unreasonable, and thus may correctly substitute its own just and reasonable market rule. Milford/NRG further state that the April 16 Order does not alter the Market Monitor's role or impose an undue burden on the Market Monitor; rather, it simply requires the Market Monitor to divulge the results of the cost review that it would have performed under ISO-NE's proposed rule as well, and to permit a generator to submit a revised bid based on that review. Thus, Milford/NRG claim, ISO-NE's claim that the Commission's ruling improperly expands

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[41] *Id.* at 24.

[42] *Policy Statement on Market Monitoring Units*, 111 FERC ¶ 61,267 at P 3 (2005), cited at ISO-NE request for rehearing at 25 n.55.

[43] NECPUC request for rehearing at 16, *citing* April 16 Order at P 117 ("the compensation received by the de-listed resource may not allow it to recover costs that might otherwise be avoided or not incurred if the resource were not subject to the obligations of a listed capacity resource [and this] result . . . may act as a disincentive for de-listed resources to participate in Forward Capacity Auctions and the FCM").

the Market Monitor's role is unjustified. Milford/NRG questions the Commission's determination that ISO-NE's original proposed rule could result in confiscatory ratemaking, and that ISO-NE's concern regarding price searching is unfounded. Milford/NRG state:

> ISO-NE's position fails to acknowledge that generator owners, with valid economic reasons for removing a generating unit from the market, may have legitimate bases for differing with the Market Monitor regarding appropriate or necessary costs associated with staying in operation, and that, as a general matter, design of cost-of-service rates often involves judgment, the exercise of which is no indication of market power. Even ISO-NE notes that the submission of de-list bids involves "business judgment" where it may be difficult to make an accurate estimate of costs, tacitly admitting that not all non-conforming de-list bids are evidence of bid inflation.[44]

49. Milford/NRG further note that the April 16 Order recognizes ISO-NE's concern regarding price searching behavior by requiring ISO-NE to provide evidence of any such price-searching behavior to the Commission.

2. Commission determination

50. With regard to the issue of whether the Commission properly interpreted its authority under section 205, ISO-NE misstates the extent of the Commission's authority. In acting on a utility's filing under section 205, the Commission's focus is not limited to whether the rates proposed by a utility are reasonable. Here, the Commission explicitly found that ISO-NE's proposed rule was *not* just and reasonable. ISO-NE's citation to *Cities of Bethany* v. *FERC*[45] is thus inapposite. If the Commission finds that a rate *is* just and reasonable, it cannot reject that rate on the basis that a different rate would be more just and reasonable.

51. Moreover, section 205(e) provides:

> Whenever any such new schedule is filed the Commission shall have authority . . . to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and . . . after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as

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[44] Milford/NRG answer at 11-12, footnote omitted.

[45] 727 F.2d 1131 (D.C. Cir. 1984) (*Cities of Bethany*).

> would be proper in a proceeding initiated after [the rate] had become effective. . . . At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the public utility.[46]

Thus, section 205(e) provides that, once a hearing has taken place (as has occurred here, where the parties participated in a paper hearing including protests and a response to those protests), if the Commission finds that a rate is not just and reasonable, the Commission may itself set the just and reasonable rate.[47]

52. The Commission will deny the rehearing requests of ISO-NE and NECPUC. The Commission recognizes concerns that ISO-NE's market rules, as proposed, could result in compelling an existing generating resource being required to offer capacity at a price less than its net risk-adjusted going forward and opportunity costs. These concerns raise the possibility of confiscatory ratemaking, a result that is unjust and unreasonable. Neither NECPUC nor ISO-NE has provided any evidence that the original proposed market rules preclude the possibility of confiscatory ratemaking. ISO-NE's assertion that existing generators have adequate time for challenges to, and Commission review of, all rejected de-list bids does not preclude the possibility of confiscatory ratemaking as outlined in the April 16 Order. In the April 16 Order, we offered a scenario in which an existing generator whose de-list bid has been rejected and cannot resolve the dispute with ISO-NE in the "adequate" time allotted to the parties would be forced to offer its capacity at a price below both the generator's estimate of its costs and ISO-NE's estimates of

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[46] 16 U.S.C. § 824d(e) (2000).

[47] *See Wisconsin Michigan Power Co.*, 31 FPC 1445, 1452 (1964) ("Our finding that the increased rates that are the subject of this proceeding are discriminatory does not end our adjudicatory responsibilities. Under the terms of section 205(e), whenever we find a rate to be unduly discriminatory we may determine the just and reasonable rate to be thereafter observed"); *see also Boston Edison Co.* v. *FERC*, 233 F.3d 60, 64 (1st Cir. 2000) ("In regulating electricity rates, the Federal Power Act follows (with variations) a well-developed model: the utility sets the rates in the first instance, 16 U.S.C. § 824d(a), subject to a basic statutory obligation that rates be just and reasonable and not unduly discriminatory or preferential, *id*. §§ 824d(a)-(b). FERC, which inherited the powers of its predecessor (the Federal Power Commission), can investigate a newly filed rate (section 205, *id*. § 824d(e)), or an existing rate (section 206, id. § 824e(a)), and, if the rate is inconsistent with the statutory standard, order a change in the rate to make it conform to that standard, *id*. §§ 824d(e), 824e(a)-(b)").

those costs.[48] ISO-NE and NECPUC have offered no evidence that such a result will not occur.

53. We disagree with ISO-NE that our ruling violates the provisions of the Settlement Agreement and improperly broadens the role of the Market Monitor. First, the Settlement Agreement does not preclude the Market Monitor from disclosing its own estimates of the net-risk adjusted going forward and opportunity costs of an existing generator.[49] Second, ISO-NE attempts to categorize the Market Monitor's role as strictly "reviewing" in nature, *i.e.*, that the Market Monitor has no active role in the process. However, in ISO-NE's proposed market rules, not only did the Market Monitor "review" de-list bids, the Market Monitor also would reject improper bids and enter a zero bid on behalf of any existing generator that submits a bid inconsistent with its costs. Our ruling only requires the Market Monitor to submit its cost estimates to existing generators whose de-list bids have been rejected, and removes the requirement to submit a zero bid on behalf of such generators. The Settlement Agreement did not explicitly limit the Market Monitor's role to a passive, unproductive "review" of de-list bids that would not lead to any action, and ISO-NE's original proposed market rules did not limit the Market Monitor's role in such a way either.[50]

54. We also disagree with ISO-NE that our ruling improperly shifts the burden of proof from the proponent of the rate to ISO-NE in a way not contemplated by the

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[48] April 16 Order at P 118-119.

[49] In fact, the Settlement Agreement specifically provided that the implementation details of the Market Monitor's activities would be provided in the market rules:

> **Review by Market Monitor**. In reviewing [de-list] bids from Existing Capacity that are subject to review as set forth in Part III.D above, the Market Monitor shall review that the proposed bid is consistent with the Resource's net risk-adjusted going forward and opportunity costs. . . . The details of this review shall be developed in the Market Rules.

Section III.E of the Settlement Agreement.

[50] We note that, on June 21, 2007, we issued an Advance Notice of Proposed Rulemaking (ANOPR) that, among other things, solicits comments on market monitoring policies, including those related to the mitigation functions performed by some market monitors. *Wholesale Competition in Regions with Organized Electric Markets*, 119 FERC ¶ 61,306 (2007). Depending on the policy ultimately adopted, the final order in the rulemaking docket might necessitate an adjustment to the functions of the Market Monitor approved in this proceeding.

Settlement Agreement. The "proponent" of the rate, *i.e.*, the existing generator, must submit its de-list bid to ISO-NE for approval. In order for the Market Monitor to judge whether that bid is consistent with the generator's net risk-adjusted going forward and opportunity costs, as provided by the Settlement Agreement, the Market Monitor must of necessity develop its own estimate of that generator's costs. The combination of the Market Monitor's estimates results in a de-list bid that is consistent with the Market Monitor's estimates of the existing generator's costs. At that point, the existing generator may either submit a new de-list bid consistent with the Market Monitor's determination, or challenge the Market Monitor's estimates in the November Filing with the Commission. It is true that the Market Monitor must provide support for its determination of the de-list bid as inconsistent with the existing generator's costs. However, this is no different from the result that could have occurred under ISO-NE's original proposed rule: if a generator challenged the Market Monitor's rejection of its de-list bid before the Commission, the Market Monitor would have been forced to file its estimates and support for those estimates of the existing generator's costs. In other words, under ISO-NE's original proposed market rules, the Market Monitor would have essentially the same "burden" that the Commission has imposed – that is, the Market Monitor is required to provide support for its rejection of any de-list bids if that rejection is challenged.

55. Similarly, we disagree with ISO-NE and NECPUC that our ruling relieves an existing generator of the burden of proving that its de-list bids are consistent with its costs. An existing generator wishing to de-list must, in the first instance, provide its estimates of its costs with its de-list bid for approval by the Market Monitor. If the bid is unsupported, *i.e.*, the generator has failed to meet its burden, the bid will be rejected by the Market Monitor. The existing generator must then choose between accepting a lower de-list bid consistent with the Market Monitor's estimates of its costs or to appeal to the Commission in the annual November Filing. In either case, the existing generator must support its de-list bid with the knowledge that a bid that is inconsistent with its supportable cost may result in the Market Monitor's disallowance of that de-list bid.

56. In fact, if a generator does not support its bid, the generator may be forced to accept a price below its original de-list bid.[51] Because the process of arriving at that

[51] As an example, assume that a generator submits a de-list bid of $10 (a bid that reflects its actual going forward costs, but the generator carelessly fails to support the bid. Suppose that the Market Monitor inaccurately determines, due to incomplete information, that a de-list bid consistent with that generator's costs would be $8. If the generator then submits a new de-list bid of $8, but the auction clears at $9, the generator must accept that $9 price despite its initial desire to de-list at $10. Alternatively, if the generator declines to submit a new de-list bid after the Market Monitor's review, then it will still be

(continued…)

determination may well involve a certain amount of negotiation and information exchange between the Market Monitor and the generator in question, the generator will have an incentive to be as candid as possible with the Market Monitor, so as to most strongly support its own evaluation of its costs. Further, ISO-NE is incorrect in stating that because under the Commission's proposal a generator will never be required to participate in the auction as a price taker, that generator has no incentive not to inflate its initial de-list bid above its actual costs. A generator that lacks market power will have no incentive to inflate its bid above its going forward costs. That is because an inflated de-list bid by a generator lacking market power would not significantly increase the market price, and therefore, the generator would not profit from inflating its de-list bid. Indeed, the generator would risk losing profit to the extent that the clearing price is above its actual going-forward costs, since at such a clearing price, the generator would have been removed from the supply stack but would have received earned net revenue if it provided capacity at that price.

57. Further, we clarify here a point that the parties may have misunderstood with regard to the nature of the rule change that the Commission required in its April 16 Order. Based on its request for rehearing, it appears as if ISO-NE believes that, under the change required by the Commission, a generator whose initial de-list bid is rejected by the Market Monitor will have multiple opportunities to refine its bid – first, in the form of a revised de-list bid based on the Market Monitor's estimate of its costs, and second, in a challenge to the Market Monitor's estimate before the Commission, once the Market Monitor makes its informational filing regarding rejected de-list bids 90 days prior to the auction.[52] This is an incorrect understanding of the Commission's intention. We clarify that we are requiring ISO-NE to amend its proposed market rules to provide that a generator whose de-list bid is rejected by the Market Monitor may either (a) submit a new de-list bid based on the Market Monitor's estimate of its costs, in which case it

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forced to accept whatever price the auction clears at, precisely as if it had never submitted a de-list bid in the first place.

[52] *See* ISO-NE petition for rehearing at 6-7 ("[i]f a generator has the discretion to substitute the [Market Monitor]'s determination of an appropriate bid level for the generator's original bid, subject to review by the Commission, a generator will know that it has multiple opportunities to revise its bid and avoid rejection. Its first bid may, without consequence, include cost components that the generator may know cannot be justified, and that the [Market Monitor] must then discover and revise. If the [Market Monitor] does not have complete information relevant to the bid, the generator may then question the [Market Monitor]'s revised bid when the ISO submits its informational filing with the Commission. In essence, a generator will have multiple chances to refine its bid, perhaps ultimately arriving at a lower de-list bid than submitted, but still higher than the true cost").

relinquishes its ability to challenge the Market Monitor's estimate before the Commission, or (b) not submit a new de-list bid, but retain its ability to challenge the Market Monitor's estimate before the Commission. Should the generator choose the latter alternative, it bears the attendant risk that if the Commission upholds the Market Monitor's determination or otherwise concludes that the appropriate bid is below the generator's desired bid, the generator will be required to participate in the auction at a bid level determined by the Commission as just and reasonable.

58. The Commission disagrees with ISO-NE's assertion that energy market mitigation is dissimilar to capacity market mitigation because energy market mitigation involves a mechanical formula while capacity market mitigation involves subjectivity. Under ISO-NE's original proposal, the Market Monitor would have been responsible for subjectively determining proper cost estimates and bid levels for existing generators wishing to de-list. Without such estimates, however, "review" of a de-list bid for approval would be impossible. Our ruling does nothing to change this, nor does it require any additional subjective analysis on the Market Monitor's part. We are only requiring the Market Monitor to disclose its estimates of costs and proper bid levels to the affected existing generator.

59. Regarding NECPUC's argument that the Commission erred in concluding that ISO-NE's proposal would act as a disincentive for existing generators to participate in the Forward Capacity Market, the Commission notes that the April 16 Order stated that ISO-NE's proposal only "may" act as a disincentive.[53] The April 16 Order did not rely on the argument that the proposal may act as a disincentive to existing generator participation in the Forward Capacity Market, nor was it necessary to rely on such an argument as a basis for finding ISO-NE's proposal unjust and unreasonable. That said, it is in fact possible that ISO-NE's proposal could act as a disincentive for participation by existing generators in the Forward Capacity Market. Under ISO-NE's proposal, an existing generator faced the possibility of being forced to offer its capacity at a price lower than its costs. Consequently, that existing generator would have an incentive to submit a Permanent De-List Bid, *i.e.*, a bid to exit the Forward Capacity Market permanently, rather than another type of de-list bid that would only remove it from offering capacity in the next Capacity Commitment Period.

60. The Commission recognizes ISO-NE's and NECPUC's concern that our ruling may provide an incentive for price searching behavior by existing generators. Nevertheless, the possibility of confiscatory ratemaking inherent in ISO-NE's proposal is unjust and unreasonable, and the Commission will not approve a rule with the potential for that effect. However, the Commission will encourage ISO-NE and the Market

[53] April 16 Order at P 117.

Monitor to monitor bidding behavior by existing generators with respect to the exercise of market power and price searching. To that end, and as we elaborated in the April 16 Order, we will require ISO-NE "to include, in the informational filing to be made 90 days prior to the Forward Capacity Auction, an analysis of evidence, if any, of price searching behavior on behalf of existing generating capacity resources."[54]

61. Finally, we will reject NECPUC's request for revisions to the market rules to require ISO-NE to file all cost support provided by an existing generator whose de-list bid has been rejected by the Market Monitor. Existing generators are expected to provide to the Market Monitor support for its estimates of its costs in determining its de-list bid; however, that material information is provided confidentially with the expectation that it will not be made public. NECPUC's requirement would make existing generator's sensitive, material, confidential information public. Such a result is unjust and unreasonable. We will therefore require ISO-NE, when making its informational filing 90 days prior to the auction regarding de-list bids rejected by the Market Monitor, to include only that information on which the Market Monitor relied in making its determination. This will be necessary so that, if a generator chooses to challenge the Market Monitor's rejection of its de-list bid, the Commission will be able to evaluate the Market Monitor's determination, rather than having to determine the propriety of the generator's costs *de novo*. Further, we will require ISO-NE to make that filing in a manner that appropriately protects the confidentiality of that information.

B. The Commission grants rehearing to find that, when ISO-NE rejects a de-list bid for reliability reasons, it should notify the de-list bidder at the later of (i) the time during the auction that the auction price reaches the price of the generator's de-list bid, or (ii) the time when ISO-NE has determined that the de-list bid must be rejected for reliability reasons.

62. ISO-NE's proposed rules at section III.13.2.5.2.5 provide that a generator whose de-list bid clears in an auction round, but which ISO-NE determines cannot be allowed to de-list for reliability reasons, will not be informed that its de-list bid has been rejected until the conclusion of the auction. Some protesters argued that ISO-NE should inform a resource earlier if its de-list bid cannot be accepted. ISO-NE responded that it was not always possible to inform a generator that it might be needed for reliability, prior to determining whether the resource would have cleared in the auction, because the need for a specific resource might depend on what other resources clear in the auction. ISO-NE further stated that, if generators knew that they would be needed for reliability, they

[54] *Id*. at 124.

would have an incentive to seek to de-list to attempt to earn the higher of the clearing price or an RMR cost-based rate.[55]

63. In the April 16 Order, the Commission rejected the protests, stating:

> The Commission will not require ISO-NE to inform an existing generating capacity resource that its de-list bid has been rejected for reliability reasons until the conclusion of the auction. ISO-NE will be unable to determine whether a unit is required for reliability reasons until the conclusion of the auction. Only at that point will ISO-NE be able to assess the results of the auction and may determine that a resource that has submitted a de-list bid that cleared the auction is needed for reliability and cannot be allowed to de-list. Prior to that assessment, ISO-NE will not have sufficient information to make a determination that a resource seeking to de-list is needed for reliability.[56]

1. Arguments on rehearing

64. NECPUC asserts that the Commission erred in failing to require ISO-NE to modify its proposed market rules to require that, upon making a determination that it will be required to reject a de-list bid for reliability reasons, ISO-NE must notify the de-list bidder and prospective new capacity resources immediately, even if the auction is not concluded. NECPUC states that this ruling is inconsistent with the goal of the New England capacity market of minimizing the need for RMR agreements by providing incentives for new entry in locations with particular reliability needs. NECPUC states that, when the parties entered into the FCM Settlement Agreement, they intended that, if ISO-NE needed to reject de-list bids for reliability reasons, that rejection should be short-term, with alternative arrangements quickly put into place to address the reliability problem so that ISO-NE could allow the resource to de-list. NECPUC argues that, given this goal, the FCM rules should facilitate the earliest possible notification of a reliability need, so as to stimulate prompt market responses.

65. NECPUC states that it recognizes that ISO-NE may, in some cases, need to wait until the conclusion of an auction before it determines that no other resource may replace a particular unit that is seeking to de-list. In that case, NECPUC considers it appropriate for ISO-NE to wait until the conclusion of the auction to reject the de-list bid. However, NECPUC states, there is one circumstance in which ISO-NE could identify a de-list bid that it must reject before the auction closes – namely, if (a) the unit seeking to de-list

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[55] April 16 Order at P 93; *see* Transmittal at 40.

[56] April 16 Order at P 98.

meets a reliability need, and (b) there are no proposed new units or proposed new transmission upgrades that could meet that need. NECPUC states that in that circumstance, there is no justification for waiting up to six months before releasing this information. Moreover, this delay would eliminate the possibility that during that period, a market-driven solution could emerge that would address the reliability problem at a lower cost in subsequent reconfiguration auctions

66. NRG argues on rehearing that the Commission did not sufficiently explain its reasons for this ruling, stating that, although the Commission did make a finding that ISO-NE would not have sufficient information to make a determination as to whether a resource seeking to de-list would be needed for reliability until after the auction, the Commission had failed to explain the basis for this conclusion and overlooked relevant facts. Like NECPUC, NRG asserts that there are circumstances in which ISO-NE will know immediately (*i.e.*, at the end of an auction round) that it will not be able to permit a particular resource to de-list, for reliability reasons, and the Commission's failure to recognize this fact is erroneous. For these reasons, NRG asks the Commission to order ISO-NE, in that circumstance, immediately to inform a resource that it will not be permitted to de-list.

67. NRG further claims that, where a generator owns multiple generating units at the same site and the de-list bids of those units are inter-related, failure to inform a generator that one of those units will not be permitted to de-list may distort generators' decision-making with regard to their de-list bids for other units.[57] Thus, NRG claims, the Commission failed to take into account the economic harm that could result from ISO-NE's failure to inform resources as soon as possible that they would not be allowed to de-list.

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[57] NRG provides the following scenario (NRG request for rehearing at 6):

> [If] the de-list bids of multiple generating units at a single station are interrelated because the units share various common costs, and when one unit shuts down as a consequence of being de-listed the remaining units' share of the common costs will go up. These costs in turn will be reflected in higher de-list bids for the two remaining units in subsequent auction rounds. Unless the generator is informed, as soon as ISO-NE itself knows, that the de-list bid for one unit will not be accepted, the generator will be misled into bidding at higher prices than its true costs in later auction rounds because it is incorrectly assuming that common costs must be borne by only the two generating units. Should these higher de-list bids clear, inefficient auction pricing and financial harm to both the owner and the market will occur because two units for which economics dictate continued operation will be shut down.

68. In its answer to NECPUC's and NRG's arguments, ISO-NE states that notifying generators that they cannot de-list prior to the conclusion of the full auction could facilitate the exercise of market power and threaten the viability of a competitive capacity market. According to ISO-NE, waiting until the end of the auction to provide notification of whether a de-list bid will be accepted will address potential market power problems by reducing the incentive of generators to seek to de-list capacity that is essential for reliability. With regard to the possible scenario laid out by NRG, ISO-NE states that the possibility for market power would be even greater in a situation where a single owner owns multiple resources at a single site. ISO-NE states that the need to thwart the exercise of market power in the market outweighs any benefit that could be gained from providing notification to a generator that it will be needed for reliability before the auction is completed.

2. Commission determination

69. The Commission grants the requests for rehearing by NECPUC and NRG.

70. As both NECPUC and NRG acknowledge, there will be instances where ISO-NE will not know until the conclusion of an auction that (in terms of reliability), no other resource may replace a particular unit that is seeking to de-list. In that case, both NECPUC and NRG consider it appropriate for ISO-NE to wait until the conclusion of the auction to reject the de-list bid.

71. However, NECPUC and NRG contend that there are other occasions where ISO-NE will know during the auction that a particular de-list bid will be rejected for reliability reasons, as there are no newly proposed units or transmission upgrades that could address the reliability need. NECPUC and NRG maintain that under these circumstances, ISO-NE should immediately notify a resource that it will not be permitted to de-list.

72. NECPUC's basis for requesting early notification of the rejection of de-list bids reflects its desire to achieve market solutions to reliability problems – *i.e.*, earlier notification of a reliability concern will provide additional time for the market to respond appropriately (through means such as reconfiguration auctions). While it offers support for that goal, ISO-NE nevertheless argues that it must also guard against the abuse of market power, specifically addressing two potential scenarios associated with early notification of its intent to reject de-list bids (*i.e.*, prior to the end of the FCA). First, ISO-NE argues that a generator that is notified before the conclusion of the auction that its bid will be rejected for reliability reasons may submit an inflated de-list bid in order to capture the "higher of" market-based or cost-of-service payments. Second, ISO-NE states, similarly, that because annual incremental capacity needs are relatively small, a generating company with a large portfolio (including a generator with multiple units at one location) would have a strong incentive to withhold generation (by de-listing units) to increase the price in the FCM. Addressing this issue, ISO-NE asserts that "the portfolio impact of market power is far more detrimental to the capacity market and greatly

outweighs the argument in favor of providing notification to generation owners prior to the conclusion of the FCA."[58]

73. The Commission recognizes the concerns regarding the timing of the disclosure of de-list bids rejected for reliability reasons. ISO-NE is concerned that a generator that knows it is needed for reliability would have an incentive to submit a higher de-list bid than it would otherwise have submitted. While the Commission recognizes this concern, we do not see how the generator could act on the incentive once the auction has begun and the auction price has descended to the level of the de-list bid. That is because, once a generator has submitted a static de-list bid in advance, or once it offers to de-list during the auction (dynamic de-list), the generator cannot subsequently increase its de-list bid. We believe that the rule changes we direct herein will balance the need for generators to know earlier which de-list bids will be rejected for reliability reasons with ISO-NE's goals to prevent inflated de-list bids and economic withholding.

74. We realize that ISO-NE may not always know whether an existing generator is needed for reliability prior to the end of the auction. On the other hand, there may be instances when ISO-NE does know prior to the conclusion of the auction that an existing generator's de-list bid must be rejected for reliability reasons. As NRG notes, the costs and de-list bids of multiple units may be interrelated and may depend legitimately on whether one unit's de-list bid has been rejected. Therefore, we direct ISO-NE to revise its market rules at section III.13.2.5.2.5 to provide that it will notify an existing generator that its de-list bid is rejected for reliability reasons at the later of (i) the time during the auction that the auction price reaches the price of the generator's de-list bid, or (ii) the time when ISO-NE has determined that the de-list bid must be rejected for reliability reasons.

C. The Commission properly capped the amount of capacity imports over the HQ Interconnection that may be accepted in the FCM at the level of the HQI Excess

75. In determining the total Installed Capacity Requirement that ISO-NE must procure on behalf of its LSEs, ISO-NE takes into consideration potential "tie benefits," *i.e.*, assumptions regarding the amount of emergency assistance that may be available over the interconnections between New England from directly-connected control areas such as New York, New Brunswick and Quebec. As the Commission previously stated:

> According to ISO-NE, tie benefits are a result of resource and load diversity between two control areas; for example, when New York has excess resources at a time when New England's resources are tight, New

[58] ISO-NE Answer at 21.

> York resources could support New England's load to the extent that transmission constraints allow. Under ISO-NE's proposal, tie benefits reduce the amount of [the Installed Capacity Requirement] needed to ensure reliability. Thus, for example, if ISO-NE determines that it needs 30,000 MW of installed capacity in order to meet its reliability objective and it determines that tie benefits total 1,000 MW, the [Installed Capacity Requirement] would be 29,000 MW. In this case, LSEs in the aggregate would need to acquire 29,000 MW of capacity through the FCM auction. The remaining 1,000 MW of capacity needed for reliability (the tie benefit) would be assumed to be available in an emergency from the neighboring control area without capacity payments made during the FCM auction.[59]

76. The Commission has previously ruled that, because transmission interties between New England and other control areas provide these tie benefits (*i.e.*, the potential of emergency assistance from these other control areas) to the system, the parties who funded those transmission interties should be compensated for those tie benefits.[60] One of the facilities that provides tie benefits to the New England area is the HQ Interconnection, a transmission line between the New England and Quebec control areas. The HQ Interconnection is owned by a discrete group of New England LSEs (the Interconnection Rights Holders, or IRHs). In the Settlement Agreement, ISO-NE proposed that, to compensate the IRHs for the reliability benefits that the HQ Interconnection provides to the New England control area, the IRHs receive Hydro Quebec Interconnection Capability Credits (HQICCs). These are credits against the IRHs' capacity obligations and they reduce the amount of capacity that each IRH is required to provide to the New England system by the amount of HQICCs allocated to that IRH.[61] In other words, if the IRHs' capacity obligation (which, like the capacity obligation for all LSEs, is set by ISO-NE), is 2000 MW, but ISO-NE calculates that the HQ Interconnection provides 1400 MW worth of tie benefits to the New England area, then the IRHs receive credits (in the form of HQICCs) for 1400 MW worth of their capacity obligations. As a result, the IRHs would only be obligated to procure 600 MW of capacity.

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[59] *ISO New England Inc. and New England Power Pool*, 118 FERC ¶ 61,157 at P 23 (2007) (footnotes omitted) (Installed Capacity Requirement Order).

[60] *Id*. at P 30 ("since loads within New England jointly share the costs of the transfer capability, loads should jointly share the benefits of that capacity, including the tie benefits").

[61] April 16 Order at P 159.

77. In its filing, ISO-NE proposed a tariff provision that would reduce HQICCs when the HQICCs are displaced by actual capacity sales over the HQ Interconnection above the "HQI Excess," *i.e.*, the total available capacity of the line minus the value of extant HQICCs. In the April 16 Order, we directed ISO-NE to modify its filing to place a cap on the amount of import capacity contracts accepted in the auction over the HQ Interconnection. We required that cap to equal the HQI Excess, so that if the capacity of the line was 1800 MW, and 1400 MW of that capacity was allocated to HQICCs granted to the IRHs, ISO-NE could only accept 400 MW of import capacity contracts in the auction. Thus, as a result of our ruling, ISO-NE's proposal to reduce HQICCs for capacity sales above the HQI Excess over the HQ Interconnection would never be applied in practice.

78. The rationale for our directive was to conform the policy regarding HQICCs to the Commission's policy on other facilities providing tie benefits in New England. In the Installed Capacity Requirement Order, we accepted ISO-NE's proposal to place a cap on the amount of import capacity contracts accepted in the auction over interties whose costs are jointly shared by all loads in New England, namely, New York and New Brunswick AC transmission ties.[62] That cap equals the difference between the total transfer capacity of these interties and the tie benefits associated with those interties. Our rationale in the Installed Capacity Requirement Order was that loads that jointly share the costs of transfer capability should jointly share the benefits of the transfer capability, including the tie benefits and the associated reduction in the Installed Capacity Requirement. Purchasing imported capacity that reduces the tie benefit would unnecessarily increase the amount of capacity that must be purchased by customers in New England.

79. Similarly, capacity imports in excess of the HQI Excess on the HQ Interconnection would reduce the aggregate HQICCs, and thus, would unnecessarily increase the amount of capacity that must be purchased. This is because such capacity imports would not reduce the amount of capacity that must be procured from within New England. Therefore, in the April 16 Order, the Commission determined that it was reasonable to cap the amount of capacity imports accepted in the FCM auction over the HQ Interconnection in order to avoid a reduction in HQICCs, just as we capped the

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[62] Installed Capacity Requirement Order at P 27, 30 ("HQUS asks the Commission to reject the decision to include tie benefits from New York and New Brunswick AC transmission ties in the [Installed Capacity Requirement] reform process . . . . We will accept ISO-NE's proposal to set aside interface transfer capability for tie benefits. We agree with ISO-NE that since loads within New England jointly share the costs of the transfer capability, loads should jointly share the benefits of that capacity, including the tie benefits and the associated reduction in [the Installed Capacity Requirement]").

capacity imports accepted in the FCM auction over other interties.[63] Moreover, because the costs of the HQ Interconnection are shared by the Interconnection Rights Holders (IRHs) but not by all New England loads, we further concluded in the April 16 Order[64] that the tie benefits associated with the HQ Interconnection (i.e., HQICCs) should be shared by the IRHs, but not by all New England loads.[65]

1. Arguments on rehearing

80. HQUS seeks rehearing.[66] HQUS disagrees with us that our directive will provide comparable treatment to that provided on other interties. According to HQUS, the other tie owners do not collect separate transmission charges that compensate them for the reduction in capacity value that occurs from the reservation of a certain amount of capacity to provide tie benefits. Customers purchasing transmission for energy transactions from Canada to the U.S. over the HQ Interconnection, on the other hand, share in the cost of that facility through their transmission payments to the IRHs. The Commission reasoned in the April 16 Order that "the tie benefits associated with the HQ Interconnection . . . should be shared by the IRHs but should not be extended to others that do not share in the HQ Interconnection's costs."[67] HQUS disagrees, arguing that a transmission customer such as HQUS pays a share of the HQ Interconnection's costs when it pays the IRHs' individual rates, and thus, should have the right to use the HQ Interconnection for both energy and capacity. HQUS states that because the owners of the New York and New Brunswick interties do not assess separate transmission charges

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[63] April 16 Order at P 167-68 ("we conclude that ISO-NE's filing should be modified so that the maximum amount of import capacity contracts accepted in the auction over the HQ Interconnection should be limited to the total available capacity of the line minus the value of extant HQICCs. . . . .We agree with NSTAR that the issue presented here is the same as that presented in our Installed Capacity Requirement Order, and thus, a comparable policy should apply").

[64] *Id*. at P 168.

[65] In the Installed Capacity Requirement Order, the Commission noted that HQUS stated its disagreement with the methodology used to allocate HQICCs to the IRHs, and its intent to challenge this methodology in future proceedings. Therefore, the Commission stated, it would not address this issue in that order. Installed Capacity Requirement Order at P 28 n. 29.

[66] Brookfield, in its comments, makes no new arguments, but states that it also supports the arguments made by HQUS.

[67] April 16 Order at P 168.

to customers who schedule energy transactions on those interties, transmission revenues to the owners of the New York ties do not increase when there is an increase in capacity imports. By contrast, according to HQUS, transmission revenues to the IRHs do increase when there is an increase in capacity imports over the HQ Interconnection. Thus, HQUS asserts that, unlike owners of other interties, the IRHs receive compensation from importers of capacity and energy, so that these importers share in the cost of the HQ Interconnection but not the cost of other interties. Because of this difference, HQUS asserts that the IRHs should not be treated the same as those owners of other interties.

81. In addition, HQUS argues that our directive in the April 16 Order that "the maximum amount of import capacity contracts accepted in the auction over the HQ Interconnection should be limited to" the HQI Excess[68] is contrary to section 11, Part III.B.3.b of the FCM Settlement Agreement, which states:

> If the accepted Import Bids [on the HQ Interconnection] exceed the difference between the approved [HQ Interconnection] transfer limit and the approved MW of HQICCs (the "HQI Excess"), the capacity requirement for those IRH … that sold their transmission rights for the subject period will be increased by the difference between the total amount of accepted Import Bids and the HQI Excess.

82. According to HQUS, our directive also effected changes to existing rules not at issue in this proceeding. HQUS argues that section 11, Part III.B.3.b, above, simply carries forward a rule that has been in place for 15 years.[69]

83. HQUS states that the section 205 filing at the root of this proceeding, which consists of new rules needed to implement FCM, did not include any changes to the provision increasing the IRHs' capacity obligations as they sell transmission at levels above the HQI Excess, and that neither the Commission nor any party acted under section

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[68] *Id*. at P 167.

[69] HQUS does not specify this rule, but the IRHs, in their answer to HQUS' request for rehearing at 8, state that HQUS is referring to section I.2.2(l) of ISO-NE's tariff, the definition of "HQ Net Interconnection Capability Credit," which reads:

> Of an IRH for a given month is its HQICC for that month, in Kilowatts, minus a number of Kilowatts equal to (1) the percentage of its share of the Phase I/II HVDC-TF Transfer Capability committed or used by it for a UCAP Transaction for that month (plus any use during the same time period by an entity that obtained an OASIS transmission reservation from that IRH for service on the Phase I/II HVDC-TF for that same time period which was used to support a UCAP transaction), times (2) its HQICC for that month.

206. Rather, the issue arose through a protest to ISO-NE's filing from NSTAR. However, in HQUS's view, the Commission should have rejected NSTAR's protest for failing to raise this issue during the development of the rules for calculating the Installed Capacity Requirement. HQUS argues that the Commission issued an order affirming rules that carried forward the provision reducing HQICCs as capacity imports increase above the HQI Excess, a provision that NSTAR did not oppose in that proceeding.

84. In addition, HQUS contends that our directive eliminated all capacity imports over the HQ Interconnection, in violation of the principles of open access, because of two changes that ISO-NE plans to make in the near future that will reduce the value of the HQI Excess to 0 MW. The first change is to decrease the total available capacity of the line from its current level of 1800 MW to 1400 MW. The second change is to increase the level of HQICCs to 1400 MW. Once the total available capacity and the level of HQICCs match (at 1400 MW), the value of the HQI Excess will fall to 0 MW, and thus, the Commission's directive would permit 0 MW of capacity imports on the HQ Interconnection.

85. In their answers, NSTAR and the IRH Management Committee disagree with several of HQUS' points. First, the IRH Management Committee asserts that the April 16 Order does not conflict with the Settlement Agreement. The IRH Management Committee states that the Settlement Agreement requires that the sum of capacity contracts and HQICCs not exceed the transfer limit of the HQ Interconnection, and the April 16 Order brings about precisely this outcome by limiting the amount of capacity contracts to those that can be accommodated without reducing HQICCs. The IRH Management Committee also disputes HQUS's claim that the April 16 Order changes an existing ISO tariff provision, namely section I.2.2(1), which defines "HQ Net Interconnection Capability Credits," a change that HQUS argues can only be made under section 206 of the FPA. According to the IRH Management Committee, the April 16 Order does not change or remove section I.2.2(1), but instead conditionally accepts new market rules proposed by ISO-NE. The IRH Management Committee further argues that section 206 does not apply to a protest challenging a new proposal by ISO-NE or a Commission order modifying new market rules filed by ISO-NE.

86. The IRH Management Committee also disputes HQUS' claim that the April 16 Order would eliminate all capacity sales over the HQ Interconnection. The IRH Management Committee states that the HQUS claim is based entirely on speculation about what ISO-NE and the Commission might do, and that the April 16 order does not change the way that ISO-NE calculates the transfer limit or HQICC values or the process for approving those values. NSTAR states that, contrary to HQUS' position, the cap on capacity imports of the HQ Interconnection provides comparable treatment to other interties. NSTAR argues that the IRHs bear the full costs of the HQ Interconnection in the first instances, and that allowing capacity imports to exceed the HQI Excess would transfer the higher cost of capacity acquired from the FCM to IRHs while conferring a windfall on a limited number of capacity importers, such as HQUS, which have not borne

the cost of creating the tie benefit. NSTAR concludes that granting the relief sought by HQUS would transfer existing rights and benefits from customers in New England to a foreign entity.

87. HQUS filed an answer to these answers. HQUS disputes the IRH Management Committee's claim that the April 16 Order does not modify the Settlement Agreement or the ISO Tariff is incorrect. Rather, HQUS avers that tariff changes in fact will be required to implement the order's new directives. In response to NSTAR's statement that granting the relief sought by HQUS would transfer existing rights and benefits to a foreign entity, HQUS states that it is not acceptable to discriminate against HQUS simply because HQUS' parent company is a foreign entity.[70]

2. Commission determination

88. We deny HQUS' request for rehearing on this issue. Tie benefits are the benefits that can be obtained as a result of the existence of spare generating capacity in neighboring regions that become available by virtue of the transmission interconnections with those neighboring regions. These capacity benefits are available without further expense to the owners of the transmission capacity, although payments will be required for any energy that must be purchased from the capacity. As we stated in our April 16 Order, purchases of imported capacity on the interties that reduce tie benefits do not displace capacity located inside New England. Therefore such imported capacity increases the total amount of capacity that must be purchased in the aggregate by loads in New England. HQUS does not dispute this point. Furthermore, to avoid such unnecessary purchases, in the Installed Capacity Requirement Order we accepted ISO-NE's proposal to cap the amount of capacity imports that may be accepted in the FCM. For the same reason, we continue to conclude that a comparable cap on capacity imports over the HQ Interconnection is reasonable.

89. HQUS argues that a comparable policy is not reasonable because IRHs receive payments for transmission service sold to third parties seeking to sell their generation capacity to New England, while New England loads receive no additional payments for such transmission service over other interties. Thus, HQUS argues, IRHs are compensated for any loss of tie benefits resulting from third-party capacity imports, while New England loads are not compensated for the loss of tie benefits on other interties. The Commission disagrees. IRHs are not necessarily compensated fully for any such loss of tie benefits that might occur due to capacity imports. The IRHs may not decide for themselves whether the compensation they receive for providing transmission service to

[70] NSTAR sought to file a response to the response filed by HQUS. NSTAR's response provides no new information, and, as noted above, the Commission will not accept it.

third parties fully compensates for the loss of tie benefits: under their OATT open access obligations, IRHs cannot refuse to sell transmission service to third parties to the extent available transmission capacity exists on the HQ Interconnection. Similarly, transmission service cannot be refused over the other interties under the OATT to the extent available transmission capacity exists. Thus, the IRHs are required under their OATT obligations to sell transmission service to third-party customers, regardless of whether the payments for that third-party transmission service are sufficient to compensate the IRHs for any loss of tie benefits that might occur as a result of those transmission service sales. However, while the OATT prohibits transmission service denial when available transmission capacity exists, it does not guarantee that there will be a buyer for a third party's generation capacity. In the Installed Capacity Requirement Order, we accepted ISO-NE's proposal to prevent the FCM auction from accepting capacity imports above a cap over interties funded by all New England loads. We see no reason why a comparable cap should not apply to capacity imports over the HQ Interconnection, because it is not clear that the payments for transmission service received by the IRHs is sufficient to compensate them for the loss of the tie benefits that they would otherwise receive.

90. We also disagree with HQUS' assertion that the directive in our April 16 Order is contrary to section 11, Part III.G.D.b of the FCM Settlement Agreement. That section addresses the consequences that would occur if capacity import sales exceed the HQI Excess. The section does not guarantee that capacity import sales will exceed the HQI Excess. As the IRH Management Committee and NSTAR note, our directive does not overturn the Settlement Agreement's provision regarding the consequences of capacity import sales in excess of the HQI Excess; rather, the directive merely requires that such capacity imports not be accepted in the FCM auction. As the IRHs point out in their answer, HQUS' citation of section 11, Part III.G.D.b, omits the critical first sentence of that section, which reads, "[t]he total amount of accepted Import Bids over the Phase I/II tie [*i.e.*, the HQ Interconnection] plus approved HQICCs cannot exceed the approved [HQ Interconnection] transfer limit."[71] As a result of the Commission's ruling, capacity contracts in an amount exceeding the HQI Excess – namely, the amount of capacity remaining when the amount of HQICCs are subtracted from the line's rated transfer

[71] Thus, the totality of section 11, Part III.G.D.b reads as follows (*see* IRHs' answer at 7):

> The total amount of accepted Import Bids over the Phase I/II tie plus approved HQICCs cannot exceed the approved Phase I/II transfer limit. If the accepted Import Bids exceed the difference between the approved Phase I/II transfer limit and the approved MW of HQICCs (the "HQI Excess"), the capacity requirement for those IRHs or their designees that sold their transmission rights for the subject period will be increased by the difference between the total amount of accepted Import Bids and the HQI Excess.

capability – may not be accepted in the auction. The remainder of the paragraph addresses how to proceed if the Commission were to change that ruling, so that capacity contracts could be accepted in an amount exceeding the HQI Excess. Until and unless the Commission changes its ruling, that provision will remain theoretical. Nevertheless, it will remain in place and will take effect if the Commission should change its ruling with regard to capacity contracts accepted in the auction. Thus, it is inaccurate to state that the Commission's ruling changes, or is contrary to, section 11, Part III.G.D.b.

91. We also disagree with HQUS that our directive ordered changes to existing rules not at issue in this proceeding, and thus that such changes must be made under section 206 of the FPA. Our directive was in response to protests from NSTAR regarding the netting provision of the proposed rules (*i.e.*, where capacity imports in excess of the HQI Excess will be netted against HQICCs) and from PPL regarding the IRHs' obligation to provide firm transmission service over the HQ Interconnection in excess of the HQI Excess. Those protests were filed in response to ISO-NE's section 205 market rule filing. As explained in the April 16 Order, we agree with several of the problems identified in the protests, although the remedy we reached is different from those proposed by those two parties. Under section 205, it was ISO-NE's burden to demonstrate that its proposed rules were just and reasonable, and, in light of the protests by NSTAR and PPL, we found that ISO-NE had not met that burden with regard to its proposed balance between HQICCs and capacity import contracts. It was not error for the Commission to find that ISO-NE had failed to demonstrate that its proposal in this regard was just and reasonable and for the Commission to put into place a just and reasonable alternative.

92. Finally, HQUS contends that our directive would eliminate all capacity imports over the HQ Interconnection in violation of the principles of open access, because of two changes that ISO-NE plans to make in the near future. ISO-NE has not yet filed the changes described in HQUS' protest, and we will not rule on HQUS' objections based on this speculative possibility. But even if these changes are ultimately made, they do not justify changing our directive. The IRHs have an irrevocable obligation to pay for all of the support costs of the HQ Interconnection, and thus, the IRHs are entitled to the benefits of the HQ Interconnection, including tie benefits.

D. The Commission properly allowed generators to submit partial de-list bids relating to ambient air temperature at prices below two times Cost of New Entry

93. As we noted in our April 16 Order, the capability of some generators is temperature dependent, with their output decreasing as ambient air temperature increases. As a result, some generators may not be able to generate their Qualified Capacity when the ambient air temperature exceeds 90 degrees Fahrenheit, the temperature used to determine Summer Seasonal Claimed Capability, subjecting these generators to availability penalties. To address this issue, in its February 15, 2007 filing, ISO-NE proposed to allow generators to submit Static De-list Bids, at a price of 2 times the Cost

of New Entry, for capacity they expect to be unavailable at temperatures above 90 degrees Fahrenheit, subject to verification of the physical limit. ISO-NE stated that it was uncomfortable with permitting such de-list bids below 2 times the Cost of New Entry, because it could allow generators to exercise market power by constructing a supply curve of bids that could manipulate the price.

94. NRG and Milford protested the requirement that such de-list bids be at a uniform price of 2 times the Cost of New Entry. Instead, NRG and Milford proposed, such capacity should be allowed to de-list *at any price up to* 2 times the Cost of New Entry. The CT DPUC opposed the proposal of NRG and Milford. In addition, the CT DPUC argued that the ability to de-list such capacity should be restricted to resources that are designated as existing resources as of the First Capacity Auction. In the CT DPUC's view, new generation entering the Forward Capacity Auction should be designed to produce its qualified capacity at times of peak load, and offers in the Forward Capacity Auction should reflect new generators' costs for providing that reliability service.

95. In our April 16 Order, we agreed with NRG and Milford that it is unreasonable to prohibit generators from submitting de-list bids for temperature-dependent capacity at prices below 2 times the Cost of New Entry, and we directed ISO-NE to modify its market rules accordingly. We stated that if some generators can reverse the loss of temperature-dependent capacity by taking measures whose cost is less than 2 times the Cost of New Entry, customers would benefit from allowing that additional capacity to be made available at prices below 2 times the Cost of New Entry. We also disagreed with ISO-NE that its proposed rule would prevent the exercise of market power; we concluded that allowing generators to submit lower bids would help to lower capacity prices. We also rejected the CT DPUC's proposal to restrict the ability to make such de-list bids to resources designated as existing resources as of the First Capacity Auction. We were not convinced that new generator design characteristics would eliminate capacity limitations resulting from high ambient air temperatures. Thus, we concluded that generators should not be required to bid capacity that is not expected to be physically available into the Forward Capacity Auction.

1. Arguments on rehearing

96. On rehearing, NECPUC protests that we arbitrarily rejected ISO-NE's concerns about the possible exercise of market power and improperly ordered ISO-NE to modify the FCM Rules to permit any unit to de-list at any price based on its temperature-dependent capacity. NECPUC states that if generators were allowed to de-list at prices lower than 2 times the Cost of New Entry without Market Monitor review, it would make the de-listing option more attractive to generators, thereby increasing the quantity of such bids and increasing the possibility of the exercise of market power.

97. NECPUC also seeks rehearing of our decision to reject the CT DPUC's proposal that any de-list bids due to ambient air temperature should apply only to resources that

are existing resources as of the first Forward Capacity Auction. NECPUC argues that under CT DPUC's proposal, new gas turbine plants would have to price their poor performance at higher ambient air temperatures into their FCA bids, making them somewhat less competitive with more flexible technologies. In this way, according to NECPUC, the rules would send the correct market signals, compensating units according to their true capacity value when they are needed most.

2. Commission determination

98. We deny NECPUC's requests for rehearing of our decision to allow de-list bids for temperature-dependent at prices below 2 times the Cost of New Entry. In other markets, bid *caps* are imposed to mitigate market power, in order to prevent inflated bids from artificially raising market prices. In this docket, curiously, NECPUC argues that ISO-NE's proposed bid *floor* – set at the level of the highest permissible bid – should be used to mitigate market power. As we stated in our April 16 Order, we do not understand why allowing generators to submit lower de-list bids will increase their ability to exercise market power and raise prices, and we do not understand why ISO-NE's proposal to require generators to submit higher bids will result in lower prices. Our decision here will help keep prices lower than otherwise would be the case, because it will allow generators that can reverse the loss of temperature-dependent capacity at a cost below 2 times the Cost of New Entry to reflect that cost in their de-list bids.

99. However, NECPUC may have misunderstood our April 16 Order to have eliminated the requirement for the Market Monitor to verify the physical limits of the temperature-dependent capacity. We clarify that our April 16 Order accepted the requirement for verification of the physical limits of temperature-dependent capacity. Thus, we require that the market rules must be modified to permit generators to submit static de-list bids at any price up to 2 times the Cost of New Entry, subject to verification of the physical limits of the temperature-dependent capacity. The verification requirement will help to address concerns about market power and ensure that the capacity associated with the de-list bid is actually temperature-dependent.

100. We also deny NECPUC's request for rehearing of our rejection of the CT DPUC's proposal that any de-list bids associated with temperature-dependent capacity should apply only to generators that are existing resources as of the first Forward Capacity Auction. To the extent that new generators cannot eliminate capacity limitations due to high ambient air temperatures, it would be unreasonable to require generators to bid capacity that is not expected to be physically available into the Forward Capacity Auctions. Indeed, such a requirement could reduce reliability, because the temperature-dependent capacity that would be purchased in the Forward Capacity Auction would not actually be available during peak periods. To the extent that new generators can eliminate the capacity limitations due to high ambient air temperatures (such as by installing inlet chilling), there are likely to be additional costs of doing so. However, there is no guarantee that the additional costs associated with eliminating these capacity

limitations are cost-effective compared to the costs of acquiring capacity from other resources. It would be more efficient for individual project sponsors to decide whether such investments are cost-effective, rather than to mandate the investments by rule.

E. The Commission ruled properly with regard to the interaction of FCM and the Interconnection Queue

101. In its February 15th filing, ISO-NE stated that during the process to develop the FCM rules, ISO-NE, NEPOOL members and other stakeholders had identified a series of policy and design issues that still required resolution. ISO-NE asserted that some of these issues represented potential improvements to the market, while others represented additions to the rules that were postponed due to the complexity of rules contained in the February 15th filing. Among those issues was the relationship between the FCM and the interconnection queue process.

102. The FCM is a forward market for physical resources and, as such, relies on output from specified resources, each of which individually must qualify to participate in the FCM. In the qualification process, ISO-NE verifies that a capacity resource is physically able to provide a level of capacity to the system. For capacity resources that have yet to be constructed, ISO-NE undertakes studies to determine whether a new capacity resource can provide incremental capacity to the system. However, there are instances in which some proposed resources will be unable to supply their full amount of capacity, because of the presence of another proposed resource that will be interconnecting at the same or similar locations. In such cases the February 15 filing proposed to qualify new generating capacity resources for FCM participation on the basis of interconnection queue position, with priority given to resources that entered the queue earlier.[72]

103. ISO-NE recognized that relying exclusively on the interconnection queue was not an ideal solution in instances of duplicative or overlapping impacts on the system from capacity additions. However, ISO-NE asserted that resolving how to assign qualification priority to capacity resources would require addressing and settling a range of related questions. Thus, ISO-NE proposed to defer the development of a solution until after the

[72] Section III.13.1.1.2.3(f). *See also* Transmittal at 65 ("If the initial interconnection analysis demonstrates that because of overlapping interconnection impacts, New Generating Capacity Resources that are otherwise accepted for participation in the FCA cannot each provide the full amount of capacity that they each would otherwise be able to provide (in the absence of the other proposed resources), those New Generating Capacity Resources will be accepted for participation in the FCA on the basis of their Queue Position, as described in Schedules 22 and 23 of the Tariff, with priority given to resources that entered the queue earlier").

Commission had acted on all of the February 15 filing.[73] Given that the interconnection queue issue was one of several issues that required resolution, ISO-NE committed to working with NECPUC and NEPOOL participants to prioritize these issues. ISO-NE proposed to make a filing by September 1, 2007 that would include a progress report on the generation interconnection queue issue and a description of the order of priority in which it would undertake other work needed to implement the FCM.

104. The April 16 Order approved ISO-NE's proposed approach to addressing the generation interconnection queue issue, finding that setting a specific timetable for resolving the matter – as proposed by the CT DPUC and others – would impose an unreasonably short period of time to resolve the issue. The Commission further found that the timetable proposed, and the effort it would entail, could divert time and resources from the task of qualifying resources to provide capacity and conducting the initial Forward Capacity Auction. Finally, the Commission added that it considered the generation interconnection queue issue to merit a position near to the top of any list of priorities.[74]

1. Arguments on rehearing

105. NECPUC filed a request for rehearing on this issue, arguing that the Commission erred by approving an anti-competitive rule without fixing a date by which to replace it. NECPUC asserts that the April 16 Order allows ISO-NE to disqualify new capacity resources from the FCA based solely on their inferior interconnection queue positions, and sets no deadline for when ISO-NE must permit new generation to compete in the FCA based solely on price considerations. NECPUC argues that the FCM rules cannot be just, reasonable, and non-discriminatory if they permit ISO-NE to conduct multiple auctions while arbitrarily eliminating viable new entrants before they are able to compete. NECPUC contends that the first-come, first-served premise of the interconnection queue, as a consequence of the April 16 Order, threatens to remain ensconced for years to come.

106. NECPUC asserts that, despite its agreement with the CT DPUC's arguments, the Commission gives too little weight to the consequences of delay. Moreover, NECPUC argues that the Commission did not address the risks that the CT DPUC identified from continued queue-based disqualification of new generation proposals beyond the second Forward Capacity Auction, which NECPUC contends could result in a capacity price for all of New England that is higher than the true Cost of New Entry (CONE). NECPUC also argues that the rules as approved in the April 16 Order impede competition by requiring load to pay an unjust and unreasonable price for capacity and ultimately erode

[73] Transmittal at 17.

[74] April 16 Order at P 68.

confidence in the FCM. Finally, NECPUC contends that the approved method defers the FCM's primary goal of allowing new capacity resources to compete with existing capacity resources. NECPUC asserts that, on rehearing, the Commission should require ISO-NE to file rules by no later than February 1, 2008, that will permit new generation resources to compete in the FCA on the basis of price, not interconnection queue position. NECPUC contends that, absent such a deadline, neither ISO-NE nor stakeholders are likely to focus the attention that will be required to solve this difficult question.

107. In its answer to NECPUC's request for rehearing ISO-NE argued that the Commission should deny rehearing. ISO-NE states that it has been working with NEPOOL and NECPUC and anticipates making a filing that will prioritize the issues still remaining to be resolved by the end of June, 2007. ISO-NE asserts that the interconnection queue issue should be resolved via the prioritization filing, which is the only way to develop a comprehensive schedule that recognizes the limited resources of ISO-NE and the stakeholders. In response to NECPUC's assertion that without a deadline parties are unlikely to focus attention on resolving the question, ISO-NE argues that the Commission underscored the importance of prioritizing the interconnection queue issue. ISO-NE further argues that should NECPUC oppose the timeline proposed in the June filing, they may lodge an objection at that time.

108. ISO-NE notes that the Commission stated that it would be desirable to have a Reliability Agreement process redesign in place before the first Forward Capacity Auction. ISO-NE also argues that it is simply not possible to take the necessary steps to implement the FCM and simultaneously redesign the Reliability Agreement and interconnection queue processes under the timelines proposed by NECPUC.[75]

109. Finally, ISO-NE asserts that the consequences of permitting new generation resources to compete in the Forward Capacity Auction on the basis of their interconnection queue position should be minimal. ISO-NE states that the current estimate of Installed Capacity Requirements for 2010/11 is expected to be relatively

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[75] ISO-NE states (ISO-NE answer at 12):

> Given the ISO's limited resources, and the limited resources of the states and NEPOOL participants, it is simply not possible to take the necessary steps to implement the FCM and simultaneously redesign the Reliability Agreement and interconnection queue processes under the timelines proposed by the State Parties. In fact, a core group of ISO staff and consultants are currently working overtime on resource qualification, preparing for the auction, and developing the related market rules and manuals. These same staff and consultants would be part of the team required to work on interconnection queue redesign and Reliability Agreement reformation.

small while the response during the Show of Interest period represented more than 17,200 MW of new capacity. Thus, ISO-NE asserts that the impact of an orderly and deliberate stakeholder process to address the interconnection queue issue should be minimal.

110. Subsequently to filing its answer, on June 21, 2007, ISO-NE and NEPOOL jointly made a filing concerning prioritization of the issues to be addressed. In that filing they stated:

> After taking into consideration the implementation of FCM and [Long-Term Financial Transmission Rights], ISO consideration and state and stakeholder review of the interconnection queue in conjunction with FCM is the highest and most complex priority going forward. . . . The current plan is that interconnection queue redesign will take place during the third quarter of 2007 through the third quarter of 2008. This schedule will allow implementation of a redesigned queue process, if approved, for application in the third [Forward Capacity Auction]. The ISO expects formulation of solutions to occur in the second quarter of 2008 and culminating in a Commission filing during the third quarter of 2008. This process will also include consideration of the question of intra-zonal deliverability, which the Commission has required the 1SO to consider and which is closely related to the interconnection queue issue in the FCM.[76]

2. Commission determination

111. First, the Commission found that the proposed provision in section III.13.1.1.2.3(f) – which relies on interconnection queue position as a determinant of which capacity resources may qualify for participation in the Forward Capacity Auctions in instances where multiple new generating capacity resources produce overlapping system impacts – did not violate the terms of the Settlement Agreement. However, the April 16 Order found that the provision was not ideal but approved its use as an initial method with the knowledge that ISO-NE and stakeholders were committed to examining an alternative approach in the immediate future. Moreover, the Commission was concerned that the timetable for resolving the issue proposed by the CT DPUC would have imposed an unreasonably short time period to develop, approve and implement an alternative.

112. In its rehearing request, NECPUC proposes a deadline, by which ISO-NE should be directed to file new tariff provisions that do away with the reliance on interconnection queue position. The Commission will not direct ISO-NE to file rules to remove or revise section III.13.1.1.2.3(f) by February 1, 2008. While the Commission is supportive of

[76] ISO-NE filing, Docket No. ER07-546-002 at 9 (June 21, 2007) (footnote omitted).

stakeholders arriving at an appropriate solution, we were persuaded that the issue was of sufficient importance and complexity to avoid imposing a timeline proposed by a minority of stakeholders. In the April 16 Order, the Commission declined to implement the timetable proposed by CT DPUC and others because we were concerned that it would not afford ample time in which to resolve the matter, particularly in view that the critical task of qualifying resources for the first time would be occurring simultaneously. We reiterate that concern here. Nonetheless, the Commission continues to view this as an important priority and we support the goal, apparently shared by both ISO-NE and NECPUC, of a solution to this matter that can be implemented for the third auction.

113. Moreover, NEPOOL and ISO-NE have now made their proposed prioritization filing, stating that they plan to engage in interconnection queue redesign from the third quarter of 2007 (*i.e.*, July through September 2007) through the third quarter of 2008, and they anticipate making a Commission filing during the third quarter of 2008. In its comments on the February 15 filing, the CT DPUC argued that "perpetuation of a queue-based disqualification procedure"[77] and delay in developing a market-based alternative would risk damage to the FCM's credibility. It is now clear, however, that ISO-NE and NEPOOL are not contemplating retention of the approved provision in perpetuity. Now that ISO-NE and NEPOOL have made their filing putting forward their proposal as to the prioritization of issues, including the interaction of the interconnection queue and the FCM auction, the Commission will not grant the relief sought by NECPUC in its rehearing petition, but rather, will evaluate the timetable put forward by ISO-NE and NEPOOL's June 21 filing in its consideration of that filing.

114. NECPUC also argues that, if the approved provision were maintained over the course of multiple Forward Capacity Auctions, the prices produced by those auctions would be unjust, unreasonable and discriminatory. The Commission does not agree. This provision in question will be invoked solely in instances of overlapping impacts. In the event that the rules remained as approved over several auctions, there is no certainty that a necessary new generating capacity resource would definitely be disqualified on the basis of its position in the interconnection queue. Moreover, NECPUC has made no demonstration that the approved provision will result in unjust and unreasonable prices or even prices above the Cost of New Entry. Finally, the Commission does not agree that the approved method prevents new capacity resources from competing against existing capacity resources. Under the approved FCM rules, new capacity resources will largely be able to compete against existing capacity resources, and the large number of parties

[77] Protest, and Comments of the Connecticut Department of Public Utility Control at 16.

filing Show of Interest forms to indicate their desire to construct new capacity are indicative of that.[78]

F. The Commission properly authorized the commencement of a stakeholder process to consider revisions to the Alternative Price Rule

115. The Settlement Agreement created an Alternative Price Rule that modifies the way that the auction clearing price is determined in instances when out-of-market bids[79] exceed the required amount of new entry and certain other conditions are met. In essence, the Alternative Price Rule creates a higher clearing price than would otherwise be established.[80]

116. Proposed section III.13.2.5.2.5(f) of the market rules provided that beginning in April 2007, ISO-NE, in consultation with stakeholders and state utility regulatory agencies, would evaluate whether to modify the treatment of de-list bids rejected for reliability reasons and evaluate whether to apply the Alternative Price Rule or a similar mechanism. The proposed rules also state that by June 30, 2007, ISO-NE will file any potential rule changes related to the treatment of such bids**.**

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[78] In its answer in Docket No. ER07-546-000, ISO-NE stated that over 17,000 MW in Show of Interest Forms were submitted prior to the first auction.

[79] Out-of-Market bids are bids that are lower than what might otherwise be expected. *See* Transmittal, February 15 filing at 27. "The ISO's [Market Monitor] will review any offer submitted by a new capacity resource below 0.75 times [Cost of New Entry]. If the [Market Monitor] determines that the offer is inconsistent with the long run average costs net of expected non-capacity revenues, then the amount of capacity associated with such offer that clears will be considered Out-of-Market Capacity for purposes of determining the applicability of the Alternative Capacity Price Rule."

[80] Settlement Agreement at 11.III.I ("Alternative Price Rule. If system-wide or in any import-constrained Capacity Zone: (a) new capacity is needed in the relevant Commitment Period; (b) the FCA is: (i) a Successful FCA or (ii) the FCA has Insufficient Competition pursuant to Part III.L.2 below but not Inadequate Supply pursuant to Part III.L.1; and (c) at the Capacity Clearing Price the purchases from the Out-of-Market Bids exceeds the required new entry, then the Capacity Clearing Price for that Capacity Zone shall be the lesser of: (1) the price at which the last New Capacity Bid withdrew from the FCA (excluding Out-of-Market Bids and bids in export-constrained Capacity Zones) minus $0.01, or (2) CONE; provided, however, that the price will be set to CONE in the event of Insufficient Competition if there are no withdrawn New Capacity Bids").

117. Several parties opposed this provision, on the basis that (a) it is inconsistent with section III.I of the Settlement Agreement, which disqualifies existing capacity whose de-list bids have been rejected for reliability reasons from eligibility for a higher price under the Alternative Price Rule; and (b) section 4A of the Settlement Agreement bars ISO-NE from making changes to the Alternative Price Rule unless ISO-NE demonstrates that the change is needed to prevent a negative effect on system reliability or security or the competitiveness or efficiency of the Forward Capacity Market or forward reserve market. According to these parties, ISO-NE has not represented that a filing contemplated in the subsection can meet this standard.

118. In the April 16 Order, the Commission denied requests to delete section III.13.2.5.2.5(f). It stated:

> We disagree that that section is inconsistent with the Settlement Agreement. Rather, it merely commits ISO-NE to a process that it could undertake, in any event, even without this provision. Even absent this provision, ISO-NE could initiate a stakeholder process to evaluate whether additional market rules need to be filed, pursuant to section 4A of the Settlement Agreement, to avoid an adverse effect on (1) system reliability or security, or (2) the competitiveness or efficiency of the Forward Capacity Market or forward reserve market. When and if ISO-NE elects to file such market rule changes, section 4A of the Settlement Agreement requires that ISO-NE demonstrate that the changes are needed to avoid these effects. We will not prejudge the outcome of these stakeholder deliberations, and we make no findings in this order about whether such additional rules are necessary.[81]

1. Arguments on rehearing

119. NECPUC asserts that the Commission erred in authorizing a stakeholder process to consider modifications to the Settlement Agreement's Alternative Price Rule, despite the Settlement's provision that no Settling Party may seek modifications before the end of the agreed upon Waiver Period. According to NECPUC, ISO-NE may not seek any modification to the fixed terms of the Settlement Agreement until September 1, 2008, the specified end of an agreed-upon waiver period. NECPUC argues that the Commission has conflated the provisions permitting limited changes to the FCM rules with the prohibition on changes to the Settlement Agreement itself. Thus, NECPUC asserts, the proposed rule that the Commission accepted would impermissibly allow a stakeholder process to consider changes to the FCM Settlement Agreement without the consent of all

[81] April 16 Order at P 91.

settling parties or a reversal of the Commission's prior finding that the existing Alternative Price Rule is just and reasonable.

120. NECPUC states that section 4.A of the Settlement Agreement precludes any changes to the terms of the Agreement itself "[f]rom March 6, 2006 through the earlier of September 5, 2008 or the date on which the prices from the second FCA become final (the 'Waiver Period')." NECPUC asserts that:

> This provision was essential to the Settling Parties' bargain because it ensured that the terms of the Agreement would not be modified until there was some minimum experience with the FCM structure. Without this absolute prohibition on changes to the firm Settlement terms, it would be possible to recast the entire agreement to the detriment of the parties' carefully balanced contract.[82]

121. NECPUC then states that "[f]or the same reasons, the criteria for applying the Alternative Price Rule must be inviolate for the duration of the Waiver Period. . . . The final package Agreement [including the Alternative Price Rule] represented a compromise that most parties considered acceptable, and any changes to the criteria for applying the Alternative Price Rule would have required commensurate compromises in other areas in order to achieve broad support."[83]

122. NECPUC further states that the only permissible process for changing the Settlement Agreement during the Waiver Period would be under (a) a Commission-initiated section 206 determination that the Settlement as approved is unjust and unreasonable, (b) unanimous agreement among all the Settling Parties that changes are necessary or (c) a section 206 filing by a non-signatory to the Settlement Agreement. NECPUC states that the Commission's interpretation of the scope of section 4.A would expand the possibilities of making changes that would disrupt the balancing of interests that enabled the parties to enter into the Settlement Agreement, and that, although the Commission has stated that it will not prejudge the outcome of the discussions regarding changes in the Settlement, by authorizing the process the Commission "tacitly gives leave for changes that would otherwise violate the Settlement Agreement" and "strengthen[s] the position of change advocates and make[s] the outcome a virtual *fait accompli*."[84]

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[82] NECPUC request for rehearing at 9-10.

[83] *Id*. at 10.

[84] *Id.* at 12.

NECPUC further states that ISO-NE has not justified an expedited process to consider expanding the scope of the Alternative Price Rule.[85]

123. In its response, ISO-NE states that NECPUC mischaracterizes section 4.A of the Settlement Agreement. ISO-NE states that that section provides, in relevant part, as follows:

> Except as provided in section 4.C, during the Waiver Period, the ISO shall retain its authority under section 205 of the FPA to file modifications of the Market Rules that address the terms of the Settlement Agreement; where the ISO makes such a filing, the ISO must demonstrate to the FERC that failure to implement the proposed change in the Market Rule would have a negative effect on (1) system reliability or security, or (2) the competitiveness or efficiency of the Forward Capacity Market or forward reserve market.[86]

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[85] NECPUC states (*id*. at 12-13):

ISO-NE must show that a rules change is necessary "to avoid an adverse effect on (1) system reliability or security, or (2) the competitiveness or efficiency of the Forward Capacity Market or forward reserve market." ISO-NE recently published all de-list bids for the first [Forward Capacity Auction]. For that first [Forward Capacity Auction], ISO-NE can consider no more than 19 de-list bids, totaling 677 MW of capacity (compared to a Power Year 2007/2008 [Installed Capacity Requirement] of 31,270 MW and 15,000 MW of new capacity that submitted Show of Interest Forms). Three bids (one permanent de-list bid, one export bid, and one static de-list bid) represented 550 of the 677 MW. The remaining 16 bids, totaling 127 MW, varied in size from 0.3 to 3 MW and principally sought de-list status for ambient air temperature reasons. None of the de-list bids was in Connecticut, the only area likely to have any reliability concerns for the first Commitment Period. Thus, it will be impossible for ISO-NE to show that any rule modification will be necessary until at least the second [Forward Capacity Auction].

[86] Settlement Agreement, section 4.1, cited in ISO-NE answer at 15-16. *See also* Explanatory Statement In Support of Settlement Agreement, March 6, 2006, at 20:

Under section 4.A., the settling parties waive their section 206 rights to seek a change in the Settlement Agreement or the Market Rules implementing the agreement for a period of roughly two and one half years (the "Waiver Period"). During this Waiver Period, subject to section 4.C., the ISO retains its FPA section 205 rights (subject to appropriate stakeholder processes) but may exercise those rights only upon a showing that the change is needed to prevent a negative effect on system operations or the forward capacity or forward reserves markets. After the Waiver Period, all Settling Parties have their rights provided by law to seek changes.

124. ISO-NE states that it is erroneous to consider this, as NECPUC does, as an absolute prohibition on changes to the terms of the Settlement Agreement, and that, instead, this provision explicitly provides that ISO-NE may make filings with the Commission under section 205 if it can demonstrate that specific negative consequences will otherwise occur. ISO-NE further argues that the question of whether changes may or may not be made to the Alternative Capacity Price Rule is not yet ripe for Commission review, because it is not yet known whether the stakeholders will recommend any changes, and whether that recommendation will require ISO-NE to seek to change the Alternative Price Rule.

2. Commission determination

125. The Commission denies NECPUC's request for rehearing. We agree with ISO-NE's interpretation of section 4.A of the Settlement Agreement, namely, that except as provided in section 4.C, during the Waiver Period, ISO-NE shall retain its authority under section 205 of the FPA to file modifications of the Market Rules that address the terms of the Settlement Agreement.[87] Thus, ISO-NE would have the authority, under section 4.A, to make a filing under section 205 to consider modifications to the Settlement Agreement's Alternative Price Rule, if it can show that the modifications are needed to avoid a negative effect on system operations or the forward capacity or forward reserves markets.[88]

[87] Section 4.C provides that the standard of review solely for challenges to the Capacity Clearing Prices and to transition provisions shall be the "public interest" standard of review under *Mobile-Sierra* (*United Gas Pipe Line Co*. v. *Mobile Gas Service Com*., 350 U.S. 332 (1956), and *Federal Power Commission* v. *Sierra Pacific Power Co*., 350 U.S. 348 (1956).

[88] Additionally, we note that ISO-NE represented that, if it sought to make changes to the Alternative Price Rule, it would make a filing doing so by June 30, 2007. ISO-NE has not made such a filing. This fact, however, does not change our ruling as to ISO-NE's authority to make the filing.

G. The Commission denies clarification with regard to the drafting of reliability agreements and with regard to the question of whether a unit seeking to retire must comply with the FCM rules for Permanent De-List Bids.

1. Retirement of units under tariff section I.3.9

a. Arguments on rehearing

126. NECPUC asks for clarification with regard to the Commission's statement that any unit seeking to retire under section I.3.9 of the tariff must first submit a Permanent De-List Bid. NECPUC states that the Settlement Agreement provides that all Existing Capacity resources will be entered into the Forward Capacity Auction unless their Permanent De-List Bids are accepted,[89] but in the April 16 Order, the Commission stated that "ISO-NE's proposed FCM Rules do not preclude or revise the current New England market rules for the retirement of resources that allow generating resources to submit notice of retirement at any time, given a notice period of sixty days and subject to a reliability review by ISO-NE."[90] NECPUC asserts that the FCM is designed to control physical withholding from the auction, and the exercise of market power, and that once a resource has accepted a capacity obligation, it is bound by that obligation and may not relieve itself of that obligation by retiring. Thus, NECPUC asks the Commission to clarify that section I.3.9 of the tariff simply provides for increased financial assurance for a unit that submitted both an accepted Permanent De-list Bid and a section I.3.9 notice of retirement, and therefore, may not be subject to the same financial assurance sanctions as other Existing Generating Resources; and thus, a resource may not evade the FCM's de-list bidding requirements and capacity resource obligations by filing a retirement notice at any time.

127. In its response to the motion for clarification, ISO-NE affirms that a resource seeking to retire must comply with the market rules associated with the FCM and cannot evade its capacity obligation. It further states that a unit that has undertaken a supply obligation in the FCM may not retire without covering that supply obligation. ISO-NE then states that:

> In no circumstances may a resource circumvent the requirement to cover a Capacity Supply Obligation by notifying the ISO that the unit is being retired. Because of the interrelationship between Reliability Agreements,

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[89] NECPUC request for rehearing and motion for clarification at 21, *citing* Settlement Agreement, section 11, part II.D.

[90] April 16 Order at P 108, *citing* section I.3.9 of the ISO-NE tariff.

> unit retirements and the FCM, as well as the need to harmonize the rules associated therewith, the market rules regarding retirement currently residing in section I.3.9 of the Tariff will be revised.[91]

128. Capacity Suppliers in their answer state that in the April 16 Order, the Commission has already rejected the notion that a unit must submit a Permanent De-List Bid to retire. According to Capacity Suppliers, the Commission found that the pre-existing tariff provision allowing resources to retire at any time was unchanged by the FCM market rules, and remained in effect. Capacity Suppliers state that this holding is consistent with the provisions of the Settlement Agreement that contemplate that units can cover their obligations through bilateral contracts or through reconfiguration options, and that retiring units may also use these options. Capacity Suppliers also point to the provision of the Settlement Agreement under which, "except where the capacity obligation has been transferred to another Resource, Existing Capacity that has been allowed to retire under section I.3.9 of the Tariff . . . shall be required to provide additional financial assurance equal to two and one half times the [Forward Capacity Auction] Payment for a month."[92] Capacity Suppliers argues that this shows that the parties to the Settlement Agreement intended to allow units to retire, and acknowledged the ability of resources to fulfill their capacity obligations even after retirement. Capacity Suppliers further notes that any retiring resource will be subject to significant financial penalties if it fails to cover its capacity obligation.

b. Commission determination

129. The Commission denies the clarification requested by NECPUC on this issue. The clarification that NECPUC requests would, in essence, vitiate ISO-NE's current rule that a resource may retire if it gives 60 days notice. ISO-NE states (and we agree) that under the current rules, if a unit that has taken on a capacity obligation seeks to retire, it must still fulfill its capacity obligation in some other fashion (*i.e.*, by contract or otherwise). (ISO-NE also notes, however, that the market rules concerning retirement will be revised to address the interaction between Reliability Agreements, unit retirements and the FCM.) On the basis that ISO-NE has confirmed that a unit may not seek to evade fulfilling its capacity obligation through requirement, it is our view that the clarification requested by NECPUC is not necessary.

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[91] ISO-NE answer at 23.

[92] Capacity Suppliers answer at 3, *citing* section 11, part IIG.2.a of the Settlement Agreement.

2. Development of reliability agreement

a. Arguments on rehearing

130. In the April 16 Order, the Commission noted that the Settlement Agreement did not address the manner in which a resource that was not allowed to de-list, because it was required for reliability, would be compensated. While acknowledging that the Settlement Agreement provided that the just and reasonable compensation for such resources should be determined by the Commission, we also stated that "[n]othing in this provision . . . precludes ISO-NE and stakeholders from proposing a methodology for determining a proposed just and reasonable rate for units needed for reliability. . . . While we will not order a date by which this filing should be made, we agree with ISO-NE that it would be desirable to have its Reliability Agreement process redesign in place before the first Forward Capacity Auction."[93] The Commission then further noted that "we will not address here the issue of what the just and reasonable compensation should be for a resource whose de-list bid is rejected for reliability reasons. Rather, when and if we are presented with a specific case in the future, we will consider the evidence presented and make our decision at that time."[94]

131. NECPUC states that the Commission erred in ruling that it would defer the issue of just and reasonable compensation for reliability units until it was presented with a specific case in the future, since there would never be a specific case until the first Forward Capacity Auction, and this goal is thus inconsistent with the Commission's earlier statement that it would be desirable to have a new Reliability Agreement in place before the first auction. It asks the Commission to clarify that, as ISO-NE determines its priorities, it must consider the Commission's urging to complete the necessary redesign for Reliability Agreements prior to the first auction.

b. Commission determination

132. The Commission denies NECPUC's request for clarification. In the April 16 Order, while we recognized that "it would be desirable to have [ISO-NE's] Reliability Agreement process redesign in place before the first Forward Capacity Auction," [95] we also stated that we would not order a date by which that filing should be made. We noted

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[93] April 16 Order at P 85.

[94] *Id*. at P 92.

[95] *Id*. at P 85.

that ISO-NE intended to pursue this redesign through its stakeholder process.[96] The clarification requested by NECPUC is unnecessary to illuminate the Commission's meaning in the April 16 Order, and we deny it.

The Commission orders:

The petitions for rehearing are hereby granted and denied, and the requests for clarification are hereby denied, as discussed above.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.

[96] We note that, in its June 21 filing, ISO-NE and NEPOOL propose that issues including the process for obtaining a Reliability Agreement, the form of the agreement, and compensation will go through stakeholder review during the fourth quarter of 2007 and first quarter of 2008, and that they anticipate making a Commission filing of tariff and market rule revisions during the second quarter of 2008. ISO-NE filing, Docket No. ER07-546-002 at 10 (June 21, 2007).